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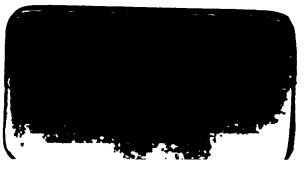

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THE NATURE OF THE CORPORATION AS A LEGAL ENTITY

WITH ESPECIAL REFERENCE TO THE LAW OF MARYLAND

BY

JAMES TREAT CARTER

A DISSERTATION

Submitted to the Board of University Studies of The Johns Hopkins University in Conformity with the Requirements for the Degree of Doctor of Philosophy

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PREFACE.

It is the aim of this study to examine the theories of the corporate entity in American Law in the light of concrete facts set forth in judicial opinions. In some measure, it is believed, the intricacies of the philosophical discussions that have agitated legal and political thinkers of Europe may be avoided in this country and thus a more settled condition in the administration of justice, and greater certainty in the status of the corporation as a legal entity in political society, may be thereby attained.

The present study grew out of an essay originally presented as a thesis at the Law School of the University of Maryland, on the subject, "The Extent to Which the Courts Will Disregard the Fiction of Corporate Existence and Deal With the Natural Persons Composing the Corporation." At the suggestion of Dr. W. W. Willoughby, Professor of Political Science at The Johns Hopkins University, and under his guidance, the study was broadened to embrace the philosophical and legal aspects of the corporate entity. The material has been gathered from legal reports and treatises in the Baltimore Bar Library, the Law Library of the Supreme Court of the United States and the Congressional Library in Washington.

For encouragement and suggestions, I am indebted to the Honorable Morris A. Soper, Chief Judge of the Baltimore Supreme Bench, and Lecturer on Corporation Law at the University of Maryland; Dr. Arthur C. Millspaugh of the Staff of Economic Advisers in the Office of the Foreign Trade Adviser, State Department, Washington; Mr. George P. Bagby, General Attorney of the Western Maryland Railroad Company and editor of the Code of Public General Laws of Maryland; and Mr. Joseph C. France. In the preparation of statistical material I acknow-

ledge the help of Charles C. Wallace, Secretary to the Maryland State Tax Commission. For his careful reading of the manuscript and suggestions relating thereto, I am under obligation to Mr. Arthur W. Machen, Jr.

Especially am I indebted, for the preparation of the graphic statistical illustrations, and assistance in compiling the data, to my wife, Irene Morey Carter. And to Major R. G. Hurlin, for his courtesy in extending to me the use of the photostat equipment of the General Staff, Statistics Branch, United States Army, I acknowledge my obligation.

September, 1919. J. T. C.

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CHAPTER I.

INTRODUCTION: SCOPE OF THE STUDY.

The legal status of the corporation today is a direct outgrowth of concepts as to its nature. Theories of corporate existence have had much to do with determining the position of the entity in law. Yet legal writers who have described corporate undertakings have not, for the most part, examined the origin of juristic doctrines, but have dealt with the more practical aspect of relations. The lawyer is primarily concerned with the rights and duties of the legal entity rather than with the source of fictions that have given rise to its present position. This is natural since it is the function of private law on its substantive side to define rights, and, on its adjective side, to designate remedies. But the real nature of the group may more clearly be determined by a preliminary examination of the constituent elements which make up corporate life.

Such an examination would begin with the interests that first impel individuals to effect an organization, and would include a survey of the characteristics of the group in operation. The essence of a thing, however, cannot be known merely by a study of its functioning at one particular time or in one particular place. Such activity represents only the reflections of a creature centuries old and the inhabitant of many continents. It is therefore necessary as well to take note of the origin of the thing, and to understand in a measure its development in relation to changing economic, social, and political conditions.

To be sure, an exposition of the nature of the corporation must necessarily include an analysis of the effects produced by it as a functioning element in society. At best, however, such an analysis is merely descriptive. For the practical viewpoint concerns itself but secondarily with the nature of the thing in itself and does not regard theories as of primary importance to

everyday business undertakings. Conclusions about the nature of a corporation, according to such a standard, are to be regarded as merely interesting explanations of the manner in which the courts have decided to view particular rights or obligations in order to dispose of a special case. Judicial decisions, however; should, and do for the most part, rest upon concepts determined by constant application of the principles of Jurisprudence and Philosophy of Law. Wherefore the judge, and, if he would have some part also in moulding the evolution of judge-made law, the lawyer as well, must look to Jurisprudence and Philosophy quite as much as to legal systems as they exist today, if he would evolve principles of law at once satisfactory to the requirements of logical reasoning and in harmony with economic conditions. Moreover, an attempt to arrive at the sources, origin, and nature of the concepts of corporate existence is a prerequisite to an adequate analytical discussion of court decisions upon the subject.

That such a study as this properly has a place in the field of Political Science may appear from a summary definition of its relation, respectively, to the Science of Jurisprudence, to Political Science, and to Law.

Those who practice law do not need to be told of the perplexing problems which confront their profession in securing a settled administration of justice. The uncertainty and lack of uniformity in state and federal court decisions makes it well-nigh impossible to advise a client concerning his rights and obligations with any degree of assurance. The result is a self-evident proposition: commerce and industry cannot ably serve the State on the shifting foundations of an uncertain legal status. Corporate organization is both necessary and convenient for men to employ. A reasonable degree of certainty and assurance that the end desired may be attained, is essential.

Where, it may be asked, can the lawyer turn for light? The nature of his profession bids him bind himself to the decisions of the courts. To him the fact of law as it exists today is final.

As a practical adviser of commercial, financial, and industrial interests, he is forced to regard it as a system conclusive, static. It needs no demonstration, however, to the men of his profession to establish the fact that all law is in constant process of modification by legislation and judicial interpretation. And no other branch of the law is more in flux than the law of corporations.

The lines of change indicate a marked tendency of the courts to modify established theories of the nature of the corporation. Where, then, shall the judge find his interpretation of the law? He must do justice as the circumstances of a case require, in the light both of precedent and sound reason. But why should sound reason so often seem to demand the modification of precedents? The answer is at hand: legal concepts have grown up that have become crystallized into a static system of law, while the expansion of commerce and industry has carried society beyond the social, economic and political conditions which gave birth to ancient theories. To be sure, the law has kept pace in great measure to this development. New fictions have been introduced to enable the courts to administer that substantial justice to which they have ever been committed. Yet, even more than law, political society is itself dynamic, and the very fictions which the beginning of a century called forth as steps in advance, have been discarded to suit a later period of economic and social development.

Herein lies the relation of corporate concepts to the Science of Jurisprudence. Jurisprudence, it may be said, is an analytical science and deals rather with the various relations which are regulated by legal rules than with the rules themselves which regulate those relations. Therefore, "Jurisprudence is not the material science of those portions of the law which various nations have in common; but the formal science of those relations of mankind which are generally recognized as having legal consequences."[1]

[1] Thomas Erskine Holland, Jurisprudence, p. 9 (12th ed.).

The controversy as to the nature of the corporate entity cannot rest with an examination of those relations of men which have legal consequences. It is necessary to go back of the science of Jurisprudence, therefore, to the Philosophy of Law. For the philosophical interpretation of the nature of the corporate entity must be constantly in the minds of the courts. The fundamental philosophic concepts upon which definitions of the corporation rest should be subjected to analysis so far as practical considerations permit. And philosophy will certainly impel us to take note of the nature of the corporate will and of group morality.

Political Science, on the other hand, is concerned with the corporate entity as a part of the State,—that "organized society, maintained under a supreme authority for the maintenance of an orderly and progressive existence."[2] General Political Philosophy, as a branch of Political Science, is interested in the nature of the corporate entity as it has developed in different countries. Particular Political Science is concerned with the examination of the corporation as it has appeared in the American system of law. It is from this last viewpoint—that is, Particular Political Science, that the last chapters of this study are undertaken; and it is from the point of view of General Political Science that the earlier chapters are written.

Lest it be thought that this study makes an unjustifiable assumption that every corporation is a political type such as may be the subject of a study in Political Science and Public Law, and lest it appear that the corporation is more rightly a subject for a study in Private Law, it is suggested that an adequate analysis of the nature of the corporation will throw light on the nature of the State itself.[3] And, quite apart from its significance in relation to the nature of the State in general, certainly the nature of the particular State within which we live may be better understood by an analysis of one of its most

[2] W. W. Willoughby, The Nature of The State, p. 2.
[3] Otto Gierke, Political Theories of the Middle Age, translated with an introduction by Frederic W. Maitland.

important constituent elements. Such an analysis obviously touches on both the domain of Constitutional Law and that of Political Science in its broader aspect. Especially is this true when the particular constituent part of a political society studied is itself of the genus of which the State is held to be the highest species.

An adequate study of the nature of the corporation must proceed in the light of comprehensive surveys that have been made of the nature of the State itself. And, indeed, any such study of the nature of the State must find its materials (as well as, in this case, its likeness), in the analysis of particular types of corporate groups within the State. If we substitute for the word "State," the word "corporation," in Dr. Willoughby's postulate as to the scope of a study of the Nature of the State, the paraphrased quotation cannot fail to indicate the striking similarity of the extent of the two inquiries. It would read as follows:

"The conception of the 'corporation,' which we have to obtain, if it is to be satisfactory, must be one that will disclose its ultimate nature, including therein a sufficient reason for its existence, and adequate justification of the right by which it exercises its authority. It must contain a statement of the attributes with which a 'corporation' is necessarily endowed, and by the possession of which it may be distinguished from other 'associations.' It will thus afford us a general type, rather than an empirical illustration. The origin of political authority (that is, 'corporate autonomy'), so far as it can be rationally determined, must receive satisfactory treatment, and the loction of sovereignty, (that is, 'group will') be considered. Furthermore, the conception must be one upon which we can base a true philosophy of law, and in accordance with which may be satisfactorily interpreted the nature of the relations between different 'corporations' (that is, 'members of the State'), and between particluar 'corporations' and the individuals composing them."[4]

[4] Willoughby, The Nature of The State, pp. 6-7. Alterations in the language of the quotation, and additions thereto, are enclosed in quotation marks or parentheses.

CHAPTER II.

DEFINITIONS AND HISTORICAL SUMMARY.

Characteristics of Corporate Existence. The most usual distinguishing characteristics of a corporation are: limited liability of individual members for the debts of the corporation, continuing existence irrespective of change of membership or stock-ownership, and centralized control of property and interests. To these may be added the necessary condition of corporate existence: origin and definition of legal powers in an enabling act of the State. A frequent, though not essential concomitant of corporate organization is large concentration of capital. This latter characteristic, however, is an economic reason for incorporation, rather than a quality usually thought of as inherent in the nature of corporate organization.

When a criterion is sought by which to draw a line between an incorporated and an unincorporated body, no one of the above-named characteristics can be taken as an absolutely certain guide. Limited liability is not such a criterion. There are corporations the liability of whose members is unlimited, and there are unincorporated companies whose members enjoy limited liability.[5] Moreover, there are numerous degrees of limited liability. Usually each member is liable only to the trustees of a bankrupt corporation or to its creditors for the debts of the corporate body, to the extent of the unpaid par value of the shares which he holds. But shareholders of national banking corporations are made liable for twice the par value of the shares held by them in addition to amounts unpaid on their subscriptions to the capital stock.

Continuous succession—that is, the capacity for transfer or transmission of shares without interruption to the continuing

[5] Arthur W. Machen, Jr., Corporate Personality, Harvard Law Review, March, 1911, p. 350.

existence and control of the corporation—is likewise not an unfailing guide to the presence of a corporate organization. Membership in some corporations is not transferable, while shares in many unincorporated companies may be freely alienated.

The right to sue and be sued, to hold property, receive and transmit it, in the corporate name is not exclusively a quality of the incorporated group. For instance, a recent act of the Maryland Legislature[6] grants to unincorporated associations the right to sue and be sued in any action affecting the common property, in the group name, whereas at common law it was necessary in a suit by or against an unincorporated association, to make each member of the group a party.

The attribute of unified control, also, is found in other types of groups than the corporation. In fact, it is far more effectively attained in the trust form of holding title than in a corporation.[7] Express trusts have been found by the experience of the past twenty-five years to be a convenient, safe, and unobjectionable method of co-operative ownership and management. This form of organization ensures a continuity of management and control that appeals strongly to investors in real estate,

[6] Laws of Maryland, 1918, chapter 419. This is somewhat similar to section 215 of chapter 471 of the Acts of 1868, codified as Art. 23, sec. 415, Code of 1904, which was not included in the revised Corporation Act of 1908. The Act of 1868 provided that, "It shall be sufficient in any suit, pleading or process, either at law or in equity, or before any justice of the peace, by or against any joint stock company or association, to describe the said joint stock company or association by the name or title by which it is commonly known, or by or under which its business is transacted." For a discussion of this Act see Littleton v. Wells and McComas Council, 98 Md. 453, and Snowden v. Crown Cork and Seal Co., 114 Md. 658. The Act of 1908 revising the corporation laws of the state changes the words "joint stock company or association," which were contained in the Act of 1868, to "corporation," and it is not until the Act of 1918 mentioned above that the rights conferred upon unincorporated associations by the Act of 1868, and the interpretations given in the 98th and 114th Maryland cases are again put into the law.—See J. C. France, Principles of Corporation Law, 2nd ed. (1914), note, pp. 21, 22.

[7] H. L. Wilgus, Corporations and Express Trusts as Business Organizations, Michigan Law Review, Vol. XIII, No. 2, p. 71, December, 1914.

which cannot be secured by a corporation with changing officers. The trustees who are the managing officers of a trust are not so likely to be changed as are the directors of a corporation. Again, the express trust affords a more economical and more convenient and flexible form of management than does a corporation. Trustees can transact business with more ease and rapidity than directors. Indeed, the development of the trust problem in the United States bears strong evidence of the advantages of the trust form over the corporate. And Maitland holds that "of all exploits of equity, the largest and most important is the invention and development of the trust. It is an institute of great elasticity and generality, as elastic, as general, as contract."[8]

Although it is true that there is no one quality or series of qualities in the absence of which a group cannot be said to be a corporation, yet the features just mentioned are those which corporate organizations usually assume. Even though the law can personify any group or succession of men whatsoever, and yet may provide that it shall not possess any one of the usual characteristics of a corporation; and, conversely, though it may declare that an association which possesses none of those characteristics shall nevertheless be personified, we need not despair of being able to recognize a corporate creature when we see it. Take, for instance, the two most distinctively corporate characteristics: limited liability and unified action and control,—those qualities which Chief Justice Marshall referred to as "immortality" and "individuality." These are the properties by which "a perpetual succession of many perons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs, and to hold property without perplexing intricacies, the hazardous and endless necessity of perpetual conveyances for the purposes of transmitting it from hand to hand. It is chiefly for the purpose of clothing the bodies of men in succession with those

[8] Maitland, Lectures on Equity, p. 23.

qualities and capacities that corporations were invented and are in use. By these means a perpetual succession of individuals are capable of acting for the promotion of the particular object, like one immortal being."[9]

Unity of control and action, therefore, continuous succession, and perpetual existence subject to the provisions of a charter, are the distinguishing features of corporate organization. They may more clearly be seen by a comparison with the distinguishing features of other forms of association, such, for instance, as the partnership.

There has been some tendency to belittle the distinction between the partnership and the corporate forms of organization. It must be said, however, that the inclination of some writers to identify the corporation as nearly as possible with the partnership and to apply to the former the rules applicable to the latter leads only to confusion and is contrary to the law.[10] There are certain advantages which a corporation presents as compared with a co-partnership. In large enterprises, the partnership has been found to be clumsy, dangerous, and insufficient. If unsuccessful it brings ruin upon all its members, because each partner is liable absolutely for all partnership debts. Any member may bind the firm by his contract, and each one has an equal voice in deciding its policy. Its capital, credit, and consequently its amount of business, are limited necessarily by the capital and credit of a very few men---the members themselves. The death of a member or the transfer of his interest dissolves the firm. Any member may cause a dissolution at any time, and the insolvency of a member renders the partnership property subject to levy of execution for his debt. Upon the death of a partner the surviving partners have the sole charge of winding up the business, and the executor of the deceased partner is not allowed to come in. A partner

[9] Trustees of Dartmouth College v. Woodward, 4 Wheat. (17 U. S.) 518, (1819).

[10] W. W. Cook, Treatise on Corporations Having a Capital Stock, 7th ed., (1913), Vol. I, sec. 6.

may withdraw his money only at a sacrifice and by long and expensive proceedings. He cannot conveniently sell his interest or borrow money upon it. New partners cannot readily or safely be admitted.

Thus, "the partnership is restricted in its capacity, dangerous in its liabilities, narrow in its exclusion of new members, too free in its mode of making contracts, and too contracted in its opportunities for withdrawal. It is becoming obsolete as a mode of doing business on a large scale."[11]

In corporations, on the other hand, the members are not generally liable for the debts of the corporate body. The amounts already invested may be lost, but the private fortunes of the stockholders are not involved. The business is done, contracts made, not by all, but by a select few, called directors. A large capital is created by the use of funds from many sources. A person may safely invest in many enterprises and yet not take part in the management nor watch the business of any one of them. The leading spirit in an enterprise may hold a majority of the stock and may admit associates, employees, or strangers as holders of a minority of the stock, and yet he will retain the management as though he were the single owner of the concern. Persons may easily buy into or retire from the enterprise. Dissolution is not brought about by death or withdrawal or dissatisfaction of a stockholder. The insolvency of a stockholder does not affect the business of a corporation. Upon the death of a stockholder his executor votes his stock and has a voice in the continuation of the business. A stockholder may sell or pledge his interest readily and intelligibly by reason of the reports, dividends, and market quotations of his stock. "The corporation is a protection in that the liability is limited; it is capable in that it renders possible the collection of a great capital; it is efficient because the directors and they alone govern its policy and its contracts; and it is convenient because it is

[11] Cook, Corporations, Vol. I, par. 6.

easy to sell or buy or pledge or bequeath one's interest in the concern."[12]

The Supreme Court of the United States sets out the advantages of the corporation over the partnership as follows:

"The continuity of the business, without interruption by death or dissolution, the transfer of property interests by the disposition of shares of stock, the advantages of business control and management by corporate directors, the general absence of individual liability, these and other things inhere in advantages of business thus conducted, which do not exist when the whole business is conducted by private individuals or partnerships."[13]

Incorporation secures first of all the benefit of limited liability. It further preserves the continuity of the partnership unaffected by the death, lunacy, or bankruptcy of the members or by other contingencies. It minimizes the dangers of a dishonest partner by setting out the agency of the directors in articles of which all persons dealing with the corporation have constructive notice. It facilitates dealing with the shares of the partners by sale, mortgage, or settlement. It affords greater facilities for borrowing, more particularly for raising money on debentures. Stockholders who lend money to the corporation are not at the disadvantage of being postponed to other creditors as an ordinary partner is who loans to the firm.

Definitions. The preliminary discussion to this point indicates the difficulty of describing a corporation in terms of characteristics that are indispensable to corporate existence, and at the same time it presents the usual features with their accompanying advantages and disadvantages. It serves to indicate the desirability as well as difficulty of adequately defining the group. As Mr. Arthur W. Machen, Jr., suggestively puts it, The orthodox American lawyer would be apt to express his

[12] Cook, Corporations, Vol. I, par. 6.

[13] Flint v. Stone Tracy Co., 220 U. S. 107, 162, (1910). And see Law Quarterly Review, April, 1895, p. 185.

idea of a corporation as "a fictitious, artificial person, composed of natural persons, created by the State, existing only in contemplation of law, invisible, soulless, immortal."[14] But, he says, it is evident that "such a definition is a congeries of self-contradictory terms. For example, a corporation cannot possibly be both an artificial person and an imaginary or fictitious person," if we are to understand artificial in its usual sense. That which is artificial is real. Moreover, if a corporation is 'created,' it is real, and therefore cannot be a purely fictitious body. And it is hard to conceive of a corporation as imaginary or fictitious and also composed of natural persons.[15] The number of contradictions contained in the orthodox doctrine, therefore, can justify us in adopting a definition only for the purposes of assuming a starting point from which to proceed with a study of the corporate entity.

A good working definition is that set forth by Chief Justice Baldwin of the Connecticut Supreme Court: "A corporation is an association of persons to whom the sovereign has offered the franchise to become an artificial juridical person, with a name of its own, under which they can act and contract, and sue and be sued, and who have accepted the offer and effected an organization in substantial conformity with its terms."[16] Even this definition is not free from perplexities. Three fundamental ideas are involved: A corporation is a new "person" in the law resulting from the acceptance of a "franchise" to become such, by an "association" of persons. This definition is, however, a distinct advance over that of Chief Justice Marshall in the Dartmouth College Case. For Marshall had followed the language used by Lord Coke in 1613 when he defined a corporation as "an artificial being, invisible, intangible, and

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[14] Machen, Corporate Personality, Harvard Law Review, March, 1911, p. 257.

[15] Ibid.

[16] Mackay v. N. Y., N. H. & H. R. R. (1909), 82 Conn. 73, 81, 72 Atl. 583.

existing only in contemplation of law."[17] Lord Coke's definition was as follows: "A corporation aggregate of many is invisible, immortal, and rests only in intendment and consideration of law. They cannot commit treason, nor be outlawed, nor excommunicate, for they have no souls, nor can they appear in person but by attorney. A corporation aggregate of many can't do fealty, for an invisible body can neither be in person nor swear; it is not subject to imbecilities or death of the natural body and diverse other cases."[18]

Another definition of the corporation with which we not infrequently meet refers to it as an artificial person, like the State.[19] When we examine the definitions of the State, on the other hand, we find it equally tersely and inadequately referred to as the "highest type of juristic person." This mutual admiration of the State for the corporation and the corporation for the State raises interesting questions of comparison of their organization and government, to which I shall somewhat later briefly refer. For the present it is sufficient to note that the corporation and the State are similar group organizations which differ principally only in size, and the presence in the State of the sovereign quality of the group will.

From all these various definitions, it may be said at least, that a corporation is an association of individuals acting as a unit, and exercising rights and powers designated by an Act of the State. In what sense this unit is a real entity separate from the individuals that compose it; how correctly it may be designated a "person"; and to what extent dogmatic or historical fictions enter into these conceptions, can only be determined by an examination of the theories underlying them and the cases in which courts have been called upon to apply them. Before this is attempted, it should prove useful to call attention to the

[17] Dartmouth College v. Woodward, 4 Wheat. 518, 636. Lord Coke's famous definition was set forth in the case of Sutton's Hospital, 10 Coke's Rep. 1, 32, (1613).

[18] Case of Sutton's Hospital, 10 Coke's Rep. 1, 32, (1613).

[19] McKim v. Odom, 3 Bland (Md.) Chancery, 418, 420 (1828).

various bases of classification of corporations in common parlance, in order not to confuse classifications which refer to relations of the corporation to its members, with those which refer to its relations to the State, or its relations to the objects and purposes of incorporation.

Classification. Having pointed out the wide range of ideas conveyed in definitions of corporations, it may help to clarify discussion if it be noted here that the classification of corporations includes numerous groups, according to the viewpoint taken. While the scope of this study covers the general concept of the corporation, it is important to bear in mind what are the various species, although only a limited discussion of their distinguishing characteristics may be undertaken.

The early writers like Kyd, Blackstone, Kent, Angell and Ames, and many subsequent authors, subdivided corporations into distinct classes. When divided with respect to the number of members, they were aggregate and sole. The corporation aggregate is composed of more than one member at a time. The corporation sole usually designates the continuous succession of consecutive holders of a particular office.[20] As regards the functions of corporations, they were described as public, such as cities, towns, levy-courts; quasi-public, such as counties and school districts; and private. Again, private corporations were subdivided into ecclesiastical and lay. Still further, lay corporations were divided into eleemosynary or charitable,[21] and civil, the latter of which included all private corporations that were created for financial profit, such as banking, insurance, manufacturing, turnpike, bridge, and canal corporations, and certain educational institutions. The term "quasi-public" seems to have been used in the older definitions to apply to the more distinctively administrative units of the State whose corporate

[20] By statute in Maryland (Act of 1894, chap. 50), the Roman Catholic Archbishop of Baltimore is made a corporation sole with capacity to take in succession both real and personal property.—France, Corporation Law, 2nd ed., 1914, p. 12, note.

[21] Fordyce, etc., v. Woman's, etc., Association, 79 Ark. 550 (1906).

life was more passive than active, and which served as instrumentalities of the State for the purposes of taxation or the administration of justice, etc., without exercising any distinctively characteristic will of their own. Today, however, the term "quasi-public" has come to be applied also to that type of private corporation known as a public-service corporation.

A classification which refers to the place of organization and source of legal power, divides corporate groups into domestic and foreign. The domestic corporation is one that has been organized under the laws of the state wherein it is doing business. The foreign corporation is one that has been organized under the laws of another state or government than that in which it is carrying on its business. A foreign corporation that has been organized under the laws of a foreign government is said to be an alien corporation. And it follows that a corporation may be regarded under certain circumstances as an alien enemy.[22]

Still another classification includes what are known as one-man companies. These are ordinary private corporations in which all of the stock happens to be owned either temporarily or permanently by one man. This classification is somewhat elastic and at times is used to include corporations in which not all, but only the great majority of shares are held in the name of one man, or in the name of his agents and under his control.

Again, with respect to the relations of the members to one another, corporations may be described as "open" or "closed," according to whether the members do or do not possess the right freely to alienate their shares.

With reference to the legality of their birth and existence, corporations are spoken of as *de jure* or *de facto,* the former having come into existence in full compliance with the creating act both in form and substance, while the latter have simply made an attempt in good faith substantially to comply with the

[22] See Daimler Co., Ltd., v. Continental Tyre and Rubber Company (Great Britain), Ltd., and another, 114 L. T. Rep. 1049, (House of Lords, 1916). This case is discussed below at pp. 94ff.

requirements of the enabling act. Both are said to be legal, as distinct from illegal, or void corporations—that is, such bodies as are in law no corporations at all because of failure substantially to conform in good faith to statutary conditions precedent to corporate birth.

In the class of "private" corporations today, are included the ordinary business or industrial, and the public-service or quasi-public. The term "ordinary business" or industrial, is used to designate all private corporations other than those whose objects make them public-service organizations, and is itself broad enough to include those of social clubs and those of the eleemosynary type.

The fundamental division of corporations designated by the terms "public" and "private" rests upon the nature of the control exercised over them by the state. The division of private corporations into "public service" and "other" (including industrial, business, eleemosynary, etc.,) rests upon the objects and purposes for which they are formed and the nature of the work they undertake, as well as their contractual relation to the state. All corporations are said to rest on a contractual basis in their relations to the state, but public corporations are a part of the state itself—that is, they are state agencies for certain purposes and it has been held that their charters do not therefore come within the provision of the United States Constitution which prohibits a state from passing any act which would impair contractual obligations.[23] When the state creates them as a branch of itself for administrative purposes they have no rights which are not rights of the state itself.[24] Consequently in this sense, the state enters into no private contractual relationship with its own public corporations.

[23] United States Constitution, Article 1, section 10.

[24] See McKim v. Odom, 3 Bland (Md.) Chancery, 407. The reasoning in this case has been superseded in large measure as to the nature of private corporations; but in the matter of public corporations the court was on more familiar ground, since all the corporations in Maryland during the colonial period were of the latter class.

It should be kept in mind that of two corporations which perform the same business and exist for the same purpose, one may be a public corporation and one a private corporation. For instance, an educational institution, such as a college, may be established, or owned as well as absolutely controlled by the state, in which case it is regarded as a branch of the state, and a public corporation. On the other hand, the state permits and often encourages bodies of private individuals to establish a college or a university and grants them corporate existence by a contractual agreement in the form of a charter defining their rights and obligations. Such an organization would be a private corporation. The fact that the state might endow the institution or subscribe to its stocks and bonds would not make it a public corporation, nor would the fact that the state owned the majority or any portion of the shares of the corporation. To a certain extent every corporation is endowed by the state with life, powers, privileges and immunities "for a public purpose." This is true in so far as it means that no corporation, public or private, is permitted to come into existence, whose objects the state would regard as injurious to the public; and the state, on the other hand, cannot force a corporation to come into existence against its will. This is certainly true as to private corporations, and as to public corporations there could be no possible exception since the will of the public corporation is the will of the state, and hence there could be no conflict between the two. Neither does the state prevent any corporation from coming into existence if it can comply with the provisions of the general incorporation laws. In Maryland, for instance, the state constitution makes it compulsory upon successive legislatures to pass general incorporation acts wherever it is possible to make the provisions of a general law apply to a class of corporations.[26] Under such laws, practically all industrial and business corporations, as well as great numbers of public-service bodies, are formed. From the nature of the relation of the

[26] Constitution of Maryland, Art. 3, secs. 33 and 48.

public corporation to the state it is evident that all public corporations are formed by special acts of the legislature.

Before proceeding to a discussion of cases it should be noted that such terms as "public," "public purposes," and "control" are used with varying shades of meaning. As used in the term "public corporation," "public" has a technical significance descriptive of the relation of the corporation to the state. It is the relation to the state, and not the object or purpose of the corporation, which is the content of the term as so used by way of contrast with the term "private," in designating one of the two fundamental classes into which corporations are generally divided. It does not necessarily involve any inference as to the activity carried on by the corporation. A private corporation by its contractual relation to the state is endowed as an entity with capacity for enjoying private rights and obligations just as free, so far as it acts within the law, from interference by the state in the exercise of its private rights and privileges, as any other person or individual. Thus, when the courts speak of "public" as compared with "private" corporations, or *vice versa*, it is the nature of the contractual relation, from the point of view of the fundamental rights of property—and now more and more, of person—to which the term "public" refers.

In another sense, however, the term "public" is constantly used with reference to one class of private corporations, the public-service corporation. And here it is plain that since the majority of the public-service corporations are, from the nature of their relation to the state, private corporations, the term "public" must refer to the business to be undertaken, and the service to be rendered to the public—that is, to the collective members of society within the state. Here the term "public" denotes the nature of the relation, not to the state acting through its legislature but to the individual members of the state in their private capacities. This relation is not one of contract, but is "public" because of the obligations set forth by the charter contract, to perform certain services for the benefit

of the public within the state. These services are public in the sense that the corporation binds itself by its charter to render certain services, when called upon, to any member of the commonwealth, under uniform stipulated conditions, to the extent of its equipment and capacity as reasonably measured by the charter stipulations and the services rendered by like organizations in similar enterprises. Thus, a railroad company which is a common carrier is a public-service corporation, but a railroad company which is not a common carrier is not a public-service corporation. In either case it is a private corporation, and not a public corporation.

We may profitably pause a moment to consider further the railroad corporation as an illustration. From the two different meanings of the word "public" above noted, it is seen that a railroad corporation, whether it be a public-service corporation or not, may be either a public or a private corporation.

The railroad as illustrative of corporate relations is particularly significant today,[27] since the "control" exercised by the federal government under act of Congress offers an illustration of another though less troublesome phase of the use of the word "public" as applied to corporate bodies—that is, "public control." Such control does not of itself alter the status of the corporation as one of the "public" or "private" species. That can only be done by altering the contractual relation of the corporation to the state. Nor does it of itself place the corporations "controlled" in the class of public-service corporations, for that is determined by the nature of the services to be performed for individual members of the public as stipulated in the charter contract with the state. But it is true that corporations are not usually of sufficient importance to render public (that is, governmental) control necessary or desirable unless their objects and purposes are already of such a nature as to make them public-service bodies. Government control

[27] January, 1919.

does not of itself alter the status of the corporation, whether a public-service or an ordinary private body.

Public control in the sense here used means legislative direction of the methods of organization according to standards which the legislature believes to be necessary to safeguard the interests of the public. It may apply to any sort of corporation or individual. But it should be remembered that this species of control is usually supervisory. It consists of administrative acts based on legislative sanctions, whether the administrative act be done by government agents or the agents of the corporation itself. It does not generally refer to proprietary control—that is, ownership. For example, the government of the United States does not at present own the railroads of the country, although, by contract, it controls them. On their financial side, they are still private, public-service corporations, whose activities are merely confined for the time being within the narrower limits stipulated by law and contract as to who shall conduct their business. Their roads are still private property controlled (that is, owned) by the corporate bodies themselves.

Another class of institutions that may well be brought to mind at this point in connection with the examination of the use of the terms "public" and "control" is that group of private corporations which are not required by their charters or by controlling legislative acts to serve any part of the public to the extent of their capacity—that is, they are not public-service corporations. They do, however, subserve "public ends"—that is, business recognized by the legislature and courts of the state as desirable and necessary to the welfare of the state. Such, for example, are the colleges, hospitals, incorporated charities, etc. They represent that class of private corporations known as eleemosynary corporations; corporations whose business or purposes are recognized to be necessary to the general well-being of an organized, civilized society. These corporations, unless they are founded and owned by the state,—unless, because of their contractual relations with the state they are "public" cor-

porations,—are private corporations; but they are not public-service corporations. This very general and broad sense of the term "public" when used in referring to their ends, signifies that their activities and the ends which they subseve are so indispensable to that portion of the community which needs and uses them, that if private corporations or associations of individuals should not of their own initiative bring them into being, the state itself would be impelled to do so. It is in this sense, then, that the state has a "public" interest in them, and encourages them "in order to promote the ends of the state." It neither exercises a proprietary nor a supervisory control over them, and its interest is simply its desire to see them prosper.

Finally, an analysis of the nature of the corporation which attempts to classify them into groups should give attention to those private corporations more and more predominant in the industrial, business and financial enterprises of the commonwealth. It is this great body of private business corporations with which the private rights of individuals are becoming more and more identified. Yet the state has never accorded such open recognition to their "public interests" as to those of the eleemosynary or public-service corporations. It is true that in a sense, as the Maryland Court of Appeals has said, the state has an interest in every body politic which it creates. It presumes that the objects and purposes of the business of industrial corporations are in harmony with the well-being of society in that they facilitate commercial and industrial intercourse. The public interest, however, which attaches to this type of corporation is in no measure identified with altruistic motives, as is the case with eleemosynary corporations, but rests upon the *laissez faire* doctrine and the competitive economic organization at the basis of the modern capitalistic state. Nor is the passive public interest which the state avows in the commercial and industrial private corporation in any way identified with its interest in those great public-service enterprises such as canals,

railroads, turnpikes, etc., to which the state usually gives an impetus by grants of broad franchises.

In conclusion of this brief survey of the various classifications of corporate enterprises, suffice it to say that over a public corporation a state has absolute powers of life and death; over a private corporation it has only such powers of control as are limited to it by the charter agreement and the objects to which the corporation is devoted. The public-service corporation is in law a private corporation subject to a somewhat greater control than eleemosynary or commercial corporations; but it is not a political subdivision of the state, and its existence does not depend wholly upon the will of the legislature; for its charter, like that of any other private corporation, is a contract subject to the protection of the United States Constitution. On the other hand, the public-service corporation cannot dispose of its franchises and wind up its business at pleasure as can an ordinary private corporation.

Historical Summary. Having outlined the characteristics of the corporation and pointed out the various classifications into which they resolve themselves, it still remains, before undertaking a discussion of the theories underlying the nature of corporate existence, to review the important historical facts which have a particular bearing upon this study.

Joint tenancy was early employed as a means of holding property for the purpose of evading the feudal burdens resulting from inheritance, such as relief, wardship, marriage, etc.[29] A similar impulse furnished the initiative from which sprang the trusts and ecclesiastical corporations.

A study of the origin of the corporation and its history in detail would not properly be included in this inquiry into its nature. But the significance of the changes that have taken place in the application of the old theories of the corporate

[29] Maitland, Trusts and Corporations, Collected Papers, Vol. III, p. 336.

entity in modern times can only be fully understood when it is remembered that the earliest—in fact, practically all corporations from the thirteenth to the end of the eighteenth centuries—were of the nature of public corporations. On the continent, for instance, they had their source in grants of special privileges, franchises, or exemptions by the feudal lords to a group of persons living together in a village. To this source can be traced the early growth of what are now our public corporations, the town or city. Moreover, the early English corporations such as the East India Company partook of the nature of the public as well as the public-service body of today, inasmuch as they exercised monopolistic franchises at the grant of the state, and performed governmental and political functions in its behalf. At a time when the exercise of monopolies was within the prerogative of the state alone, great trading companies and the chartered companies such as the Massachusetts Bay Company, The Plymouth Company, and the Company which founded Virginia and Carolina, although their governmental functions were incidental to trade and commerce, were the recipients of monopolistic powers, rights and privileges exercised at the will of the Crown and usually in derogation of the privileges and immunities of the individual members of the state.[30] This explains, possibly, the heritage of jealous watchfulness which our courts have always claimed to exercise in their dealings with corporations, particularly in the first half of the nineteenth century. And probably it accounts in some measure for the slow development of private corporations during the colonial period and the first twenty-five years of the Republic.

[30] Gerard Carl Henderson, The Position of Foreign Corporations in American Constitutional Law, pp. 12ff, Harv. Studies in Jurisprudence, Vol. II, 1918. And see John P. Davis, Corporations: Their Origin and Development, II Ch. 6, and chs. 3-5; New York, 1905.—Also, Joseph S. Davis, Essays in the Earlier History of American Corporations, Cambridge (1917) I, 41f.—And, Baldwin, Modern Political Institutions, pp. 161ff, 166, 167; and American Business Corporations Before 1789, Amer. Hist. Rev. No. 3, 453.

There were, it is true, educational, religious, social, and charitable corporations, without monopolistic features. There were even a few business corporations of a semi-public nature whose object was probably rather to permit the concentration of a large amount of capital, for undertakings which private individuals would not venture upon, such as building a wharf[31] for the furtherance of navigation, or to provide for mutual insurance against fire.[32] But the fact that the monopolistic corporation was the prevalent type during the colonial period gives us a valuable clue to the political feeling of the time with respect to corporations in general.[33]

It is sufficient to point out that the types of corporation around which the present-day theories of corporate existence grew up and became crystallized into our court decisions were either the public or the private monopolistic, and not the ordinary private, corporation of today.[34] Indeed, Chancellor Bland in Maryland, in 1829, made the statement that none other than what we now term public corporations had ever made their appearance in that state under the Provincial government.[35] And it is quite clear that not till after the first quarter of the century did railroads and other forms of public-service corporations make their appearance in any number. The phenomenal growth of the industrial corporation is a feature of the second half of the century, and was fostered by the general incorporation laws and various kinds of tax exemptions and other special privileges offered by states that vied with one another in lending impetus to new business and industrial enterprises within their respective territories.

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[31] Such, for instance, was the Union Wharf Company, formed in New Haven in 1780, and the Proprietors of the Boston Pier, in 1768.

[32] Philadelphia Contributionship for the Insuring of Houses from Loss by Fire. Smith and Reed, Laws of Pennsylvania, I, 279. Benjamin Franklin was one of its first directors.

[33] Henderson, The Position of Foreign Corporations in American Constitutional Law, Chap. II, Harvard Studies, 1918.

[34] For a list of the first incorporated business corporations in America see Harvard Law Review, Vol. II, p. 165.

[35] 3 Bland's Chancery Decisions (Maryland), 416-420.

To be sure, private corporations were not unknown before the nineteenth century. But, as Henderson points out, they were very few in number. The English East India Company was organized in 1600 and the Dutch East India Company in 1602. The latter was the first joint-stock company whose shares were bought and sold from hand to hand.[36] Justice Baldwin of Connecticut calls attention to the fact that the New London Society for Trade and Commerce United was incorporated by the Colony of Connecticut in 1731, with both a capital stock and the power to issue circulating bills of currency. The Connecticut Land Company was organized in Connecticut in 1785, and owned the entire Connecticut Western Reserve. The governor of New Jersey asked the Assembly in 1759 to establish "an incorporated company with joint stock, to the exclusion of private traders," to trade with the Indians, but nothing came of the matter.[37] It may be said, then, that during the eighteenth century private corporations for private gain were of small consequence, and it has only been during the last fifty years that the relative importance of the different classes of corporations has changed, and that private corporations for business purposes have overshadowed all other kinds. This has been due chiefly to the limited-liability feature of modern business corporations, a feature that has rendered possible the union of many persons and many contributions of capital, with a limit to their risks.[38]

Increasing Importance of Private Corporations. The increasing importance of the private industrial corporation in American law is strikingly reflected in the rapidly growing number of cases in the United States Supreme Court in which such corporations are involved. Ten years ago it was truth-

[36] Payne, European Colonies, p. 55.

[37] New Jersey Archives XVII, 219-223, cited in J. S. Davis, Essays in the Early History of American Corporations, I, 91.

[38] Cook, Corporations, Vol. I, sec. 7. And, see address of Ex-President Elliot delivered at Chicago, March 10, 1906.

TABLE I - UNITED STATES SUPREME COURT CASES INVOLVING PRIVATE CORPORATIONS

The marked increase since 1900 in the per cent of litigated cases involving private corporations reflects the rapid growth in numbers of corporations formed. The relatively small percentage of total cases reported in 1900 which involved private corporations, probably reflects the conservatism in formation of new corporate organizations during the period of financial depression in the preceding decade.

The unusually large total number of cases reported in Volumes 218 and 246 includes several disposed of without reported discussion by the Court.

Cases reported in Volume 1 Curtis include Volumes 2, 3 and 4 Dallas, and 1, 2 and 3 Cranch. Those in Volume 6 Curtis include 9, 10 and 11 Wheaton. Volumes 50 and 65 include 9 and 24 Howard respectively. Volume 78 includes 11 Wallace, and 102 contains 12 Otto.

Source of information: Decisions of the United States Supreme Court, Law Library of Congress, Washington, D.C.

Volume of U.S. report	Date of decision	Total cases reported	Cases involving private corporations	Cases involving private corporations in per cent of total
1	1790-1806	153	5	3
6	1824-1826	106	12	11
50	1850	46	8	17
65	1860	64	13	20
78	1870	62	17	27
102	1880	95	34	36
137	1890	86	29	34
179	1900	123	40	33
218	1909-1910	241	92	38
246	1917	209	119	57

fully said that it could scarcely be exaggeration to lay half of the litigation with which our courts are filled at the doors of the corporations.[39] This fact is worthy of graphic presentation. In Table I, I have analyzed and summarized the facts obtained by examining the cases decided in the United States Supreme Court from its beginning down to the present time, reported in ten standard volumes taken at periods a number of years apart. The earlier volumes are consulted at intervals of approximately a quarter of a century prior to 1850, and after that date at ten-year intervals. As Tables I and II indicate, in the earlier reports the cases included in a single volume cover several years. In the later volumes the cases reported represent the decisions rendered during a single term only, or a part of a term. The large number of cases reported in the last two volumes cited, include many disposed of in various ways without discussion by the court. In such cases the only way of knowing whether or not they involved corporations was by the title of the case.

The important thing to which Table I and the accompanying graph especially call attention is the fact that, in proportion to the total number of cases reported per volume, the cases involving private corporations increase from three per cent. to fifty-seven per cent. in the course of the century and a quarter. Cases involving private corporations in Volume I formed only three per cent. of the total number of cases reported in the course of fifteen years; while the cases which involve private corporations in Volume 246 represent fifty-seven per cent. of the total number of cases decided during only a part of one term of the court's session.

Further analysis of the nature of the cases shows that, in Volume I, all of the five cases which involved corporations grew out of transactions with Marine Insurance Companies. No public-service corporations were involved. Of the twelve

[39] G. F. Deiser, in The University of Pennsylvania Law Review, December, 1908.

cases involving private corporations reported in Volume 6, which covered the period 1824-1826, all but one dealt with banks. Of the eight cases which refer to private corporations in Volume 50 (1850), four were banks, one a fire insurance company, and two public-service corporations.

From Volume 65 (1860) on, public-service corporations, and particularly railroads, come into prominence. Ten of the thirteen cases which refer to private corporations in that volume relate to public-service corporations. Of these ten, five have to do with railroads. Three of these five turned upon the point of the validity of the bonds of a municipal corporation which had been issued in payment for subscriptions to the stock of a railroad company, and they raised the question of the power of the municipal corporation to issue the bonds. This seems to have been a frequent kind of dispute during the period of railroad expansion from 1860 to 1890.

Of the seventeen cases of private corporations reported in Volume 78 (1870), six dealt with public-service corporations. Of the remaining eleven, four involved insurance companies, six banks, and only two referred to ordinary business corporations.

The thirty-four cases mentioned in Volume 102 (1880) include eighteen public-service corporations, of which at least fourteen were railroads. Of the sixteen other private corporations, six were insurance companies, seven banks, and only three industrial or mining concerns.

In Volume 137 (1890), only nine of the twenty-nine cases involved public-service corporations. The ordinary business and industrial corporation became more frequently entangled in higher-court litigation. From 1890 on, the private industrial and business organizations began to assume increasing importance. In the twenty cases of Volume 137 which dealt with private corporations, other than public-service bodies, only three had to do with insurance companies and three with banks.

The other fourteen grew out of the affairs of ordinary industrial and business enterprises.

A similar relation holds true in the forty cases of private corporations reported in Volume 179 (1900). Of this number, seventeen were public-service bodies. Of the other twenty-three, only three were insurance companies and one a bank. The remaining nineteen, for the most part, had to do with industrial and business concerns, with an occasional piece of litigation growing out of the affairs of a mining company.

In 1910, thirty-five of the ninety-two cases in Volume 218 involved public-service corporation cases, and of the other fifty-seven, five were insurance companies, thirteen banks, and thirty-nine industrials and business organizations.

A like situation is shown in the proportion of cases reported in Volume 246 (1917). Industrials and business concerns appear in increasing numbers. Special types of private corporations such as banks and insurance companies occupy a decreasing amount of attention in the reported decisions. Railroads, however, and an increasing number of other kinds of public-service corporations keep their place of prominence in the courts along with the ordinary private corporations not public in their nature. Of the one hundred and nineteen cases in which private corporations appear in Volume 246, fifty-seven refer to public-services bodies. Of the sixty-two other private corporations, only two are insurance companies, twelve banks, and forty-eight ordinary business and industrial concerns.

The general increase in the number of litigated cases in the Supreme Court of the United States which involve private corporations of the ordinary business and industrial type, indicates the decided increase in the number and importance of these corporations as compared with other special types of private corporations such as public-service, banks, and insurance companies.

It may be said, in conclusion, that it is of increasing importance that definite and practical theories of the corporation

TABLE II - LITIGATION INVOLVING CORPORATIONS OF ALL TYPES, BEFORE THE UNITED STATES SUPREME COURT

The table indicates the increasing number and importance in litigation, of ordinary business corporations and the prominence of public service corporations in the courts. The term, ordinary business corporations, includes all private corporations other than insurance, and banking or trust companies. Among public corporations the State is not here included. Municipal corporations make up greater part of this class.

The relatively few cases involving two types of corporations have been listed only under the heading of private corporations or public service corporations, the former class taking precedence.

Source of inforamtion: Decisions of the United States Supreme Court, Law Library of Congress, Washington, D.C.

Volume of U.S. report	Date of decision	Total cases reported	Cases involving corporations				
			Private				
			Ordinary business	Banking or insurance co's	Public service	Public	Total
1	1790-1806	153	0	5	0	0	5
6	1824-1826	106	0	12	0	3	15
50	1850	46	0	5	3	2	10
65	1860	64	2	1	10	2	15
78	1870	62	2	9	6	4	21
102	1880	95	3	13	18	3	37
137	1890	86	14	6	9	3	32
179	1900	125	19	4	17	2	42
218	1909-1910	241	39	18	35	3	95
246	1917	209	48	14	57	1	120

TABLE II (GRAPHICALLY PRESENTED) - LITIGATION INVOLVING CORPORATIONS OF ALL TYPES, BEFORE THE UNITED STATES SUPREME COURT

That the ordinary private business corporation is largely a development of the second half of the nineteenth century is reflected in the fact that it does not make its appearance in the United States Supreme Court litigation until after 1850. The constantly increasing numbers in which it appears in the Court's reported decisions, bear witness to the growing importance of such corporate organizations.

Volume of report	Date of decision	Total cases reported	Ord. bus. corp'ns / Banks or ins. cos. / Pub. serv. corp'ns / Public corp'ns
1	1790-1806	153	5
6	1824-1826	106	15
50	1850	46	10
65	1860	64	15
78	1870	62	21
102	1880	95	37
137	1890	86	32
179	1900	123	42
218	1909-1910	241	95
246	1917	209	120

should be formulated if court dockets are not to be unduly clogged with corporate questions arising from an indistinct conception of the corporate entity and its various activities and relations. Not all of the cases above referred to involving corporations necessarily turn upon points of interpretation of the nature of the corporate entity. A considerable number of them, however, touch upon that subject. Table II, with the accompanying diagram, emphasizes what has been said as to the increasing importance of the ordinary business corporation. In this table the comparison is made in concrete numbers rather than in terms of percentages. The total number of cases involving private corporations and particular types are compared. Table I, therefore, should be read in conjunction with Table II.

Conclusion. In conclusion of this chapter, attention should again be called to the uncertainty and the inherently contradictory ideas in the definitions of the corporation from which we must choose to be guided. They emphasize the need of examining the theories involved in the concept of the corporate entity. The increasing number of litigated cases before the courts which involve private corporations bears witness to the steady increase of corporate activity. Attainment of clearly defined conceptions, therefore, is highly desirable if thereby may be effected in some measure a reduction of the burden placed upon the courts and the handicap of uncertainty imposed upon corporate enterprise in general. Although not all of the cases reviewed in the tables above set forth involve questions as to the nature of the corporate entity, such litigation is not infrequent. In a later chapter we may profitably take up the more important problems which the courts have to face in dealing with the corporate entity and point out the conclusions they have reached and the theories upon which their decisions rest. In the next chapter, however, there is presented a survey of the theories underlying the nature of the corporation.

CHAPTER III.

THEORIES AND CONCEPTS OF THE CORPORATION.

There are several different views of the nature of the corporation current in modern legal literature. In court decisions and treatises, the following are particularly worthy of note:

The Individualistic Theory. In the first place, the corportion is regarded as an association of individuals whose rights and duties are the rights and duties of the individuals themselves. The corporate entity is conceived of as having no rights and duties that are separate from those of the individual members of the group, although the group itself may act as a unit. This is the theory that was fostered in Roman Law. The Romans were jealous of the various groups of individuals that associated themselves together and assumed authority to act without sanction of the state. Many laws were made against illicit companies between the time of the Twelve Tables (450 B. C.) and the establishment of the Empire. Cæsar and Augustus held group activity under strict surveillance; and in the time of Gaius and Marcian, corporations could be created only under special or general legislative authority.[40]

This theory has persisted, and not a few influential writers on corporation law today insist on the narrow and unsatisfactory doctrine. Thus, Mr. Morawetz says: "It is essential to bear in mind distinctly that the rights and duties of an incorporated association are in reality the rights and duties of the

[40] Kent, Commentaries, Vol. 2, pp. 268-269. Taylor, Elementary Civil Law, pp. 567-570. Digest, xlvii, 22, 1 and 3 (Marcian); Ibid., iii, 4; 1 (Gaius).

persons who compose it, not of an imaginary being."[41] And Mr. Taylor states that there are "two meanings of the term 'corporation': the one, the sum of the legal relations subsisting in respect to the corporate enterprise; the other, the organic body of shareholders, whose acts cause the operation of the rules of law in the constitution. These two conceptions include all that is really connoted by the term in whatever sense used."[42]

The influence of this view of the corporation is found in decisions of the United States Supreme Court. It is useful and it does not altogether preclude the possibility of joining with it the view that recognizes the essential reality of the separate corporate entity. Such a combination of viewpoints emphasizes the closeness of the individuals in the group to the entity itself. Thus, in the case of the United States v. Trinidad Coal and Coking Company,[43] the court said: "The words 'association of persons' are often, and not inaptly, employed to describe a corporation. An incorporated company is an association of individuals acting as a single person, and by their corporate name. As this court has said, 'private corporations are but associations of individuals united for some common purpose, and permitted by law to use a common name, and to change its members without a dissolution of the association.' "[44]

Judge Baldwin, in the Connecticut Supreme Court, emphasized this view of the corporation as fundamentally an association of individuals. He described a corporation as "an association of persons to whom the sovereign has offered a franchise to become an artificial, juridical person, with a name of its own, under which they can act and contract, sue and be sued, and

[41] Morawetz, Private Corporations, 2nd edition, Preface and sections 227-231. And see the quotation from this author in Judge Minshall's opinion in State v. Standard Oil Co., 49 Ohio St. 137 (1900). See also note in Wilgus, Corporation Cases, p. 100, and, Wilgus, Corporations and Express Trusts, Michigan Law Review, Vol. XIII, No. 2, Dec., 1914.

[42] Taylor, Private Corporations, Preface, and secs. 48-51.

[43] 137 U. S. 165 (1890); 34 L. Ed. 643.

[44] Citing B. and O. Rd. v. Fifth Baptist Church, 108 U. S. 317, 330.

which have accepted the offer and effected an organization in substantial conformity with its terms."[45]

A very recent writer, Mr. Gerard C. Henderson, who makes a careful analysis of the position of the foreign corporation in United States Constitutional Law, seems to revert to this theory as the one most nearly descriptive of the corporate group. He describes the corporation as merely a legal device conveniently to achieve practical juristic results. This device, he says, "is not a conception of any inherent philosophic quality in the group,—of any group will, or group organism. It is no more than a convenient technical device. The interests which it is designed to protect are of course real just as those of the individuals which compose the group are real."[46] To attribute to the corporate "personality" any sort of reality seems to Mr. Henderson the most misleading anthropomorphism. In his denial of the possibility of corporate personality, however, it seems to me that he unnecessarily casts aside the reality of the corporate entity in the desire to emphasize the feature of association among the individuals. Moreover, juristic personality, it may well be pointed out, is not necessarily anthropomorphic.

The group, says Henderson, comes into relation with outsiders, and their interests, or the interests of the public at large, may require protection. Here, a complicated system of individual duties imposed on the members of the group might be devised to protect these interests. But to achieve the practical results desired, of unity of action, continuity of policy, and limited liability on the part of the owners coupled with full liability of group assets, and yet retain the mechanism of individual rights and duties, would require a system so intricate that for practical juristic purposes it would be unworkable. To protect the group interests as well as the interests of outsiders, more adequately and with less waste of legal effort, the cor-

[45] Henderson, The Position of Foreign Corporations in American Constitutional Law, p. 167.

[46] Mackay v. N. Y., N. H. & H. R. R. (1909), 82 Conn. 73, 81; 72 Atl. 583.

porate device, he says, has been contrived, by which "the rights and duties of the members of the group with respect to a given transaction are replaced by a single set of rights and a single set of duties." This view seems to combine the theory of the corporation as merely a group of individuals with the theory (stated below as the sixth theory of the nature of the corporate entity), that the essence of corporate life lies in the relations which constitute the group and the rights and duties which attach thereto.

It should be pointed out, before leaving the discussion of Mr. Henderson's interpretation, that, if Mr. Gray's view of the nature of a right be accepted,[47] and the existence of a right be considered as necessarily involving the possibility of exertion of initiative by the holder—that is, the exercise of will to determine action,—then the description of the corporate entity as the sum of the group rights and duties, necessarily infers that the existence of group rights depends upon the exercise of a group will, and the denial of personality in the group seems, therefore, somewhat inconsistent with the definition.

In conclusion of the discussion of this first theory of the corporation, it may be said that it is not strange that this conception should have been identified with the earliest appearance of the corporation. The interests of the individuals were the primary concern, and the collective rights and duties of the group were of secondary development. The range of individual interests was far wider than that of the group, while group activities were narrowly restricted. Nor is it strange that this conception should have persisted in modern times, for even a theory which grants reality to the corporate entity, or one which endows it in addition with personality, may lead its followers into a maze of absurdities if it be sought to deduce from the separate-entity idea a condition of absolute divorce from the individuals that constitute the group to which the entity attaches. No matter how real and distinct the corporate entity may be in the rights and duties

[47] John Chipman Gray, Nature and Sources of Law, Chap. 1.

which attach to it, it is never an inconsistency to say that the corporation is always an association of individuals acting together as a unit in the group name. If the proceeding of the courts in cases where it is said that they will strip off the corporate mask and penetrate through the disguise of corporate forms,[48] seems still to champion the individualistic doctrine, it does not, in its proper sense, exclude the separate-entity theories discussed below. If the pronouncements of the courts in these cases add strength to the view that a corporation is a collection of individuals, it does not detract from the view that it is also a distinct legal entity. Indeed, it is not possible in any well rounded and complete conception of corporateness to disregard, or minimize, or, for every purpose, to subordinate the one to the other.

Our conception of corporateness has been a developing one. The fact of incorporation long antedated the explanation or definition of it in English common law.[49] By Coke's time, and somewhat before, it was understood to be an artificial person, created "by the policy of man" and granted certain capacities. Coke so declared it.[50] And he was followed by Hale[51] and by Blackstone.[52] Kyd accepted this view,[53] but placed especial emphasis upon the conception of a corporation as a collection of many individuals.[54] In the Dartmouth College case[55] both these ideas appear, per Chief Justice Marshall at page 634, per Justice Story, at page 666; and with them a third—the corporation as a franchise, per Justice Washington, at page 661. The latter view had already been announced by Blackstone,[56] and

[48] See article, Scope and Limits of the Corporate Entity Theory, G. E. Canfield, 17 Columbia Law Review, 128-143 (Feb., 1917).
[49] Wilgus, Corporation Cases, pp. 74-77.
[50] 1 Institutes, 2a, 2522.
[51] Anal., sec. 22.
[52] 1 Com. 467, 468.
[53] 1 Corp. 13, 15.
[54] 1 Corp. 13.
[55] 4 Wheat. 518, 634.
[56] 2 Com. 37.

by Kyd.[57] It was developed by Kent [58] and others.[59] Mr. Morawetz laid new emphasis upon the element of corporateness earlier pointed out by Kyd. The truth of the matter seems to be that the changing necessities of the case have caused courts and writers at various times to rely upon sometimes one, sometimes another, of these necessary parts of a complete conception of the corporation as a legal thing. Thus, at different times they have given particular prominence to different phases of corporate existence as the circumstances have required.

The Corporation as a Juristic Person. To continue the discussion of various theories in the general chronological order in which they seem to have made their appearance in Jurisprudence, we may state that a second view regards the corporation as an entity to which rights and duties attach which are different and distinct from those of the individual members. The group is accorded real existence separate and apart from that of its members. The rights and obligations which attach to the legal entity, to be sure, are similar in kind to those which characterize a natural person in law. Both the corporation and the human being might be, in this sense, "juristic persons." However, the group entity, as distinct from a natural person, is said to be properly referred to as a special kind of legal person, a "juristic person." This concept comes from the continental school. In the first half of the nineteenth century Savigny was its spokesman in Germany. It was generally accepted in French law until quite recently. Savigny undertook the scientific or metaphysical consideration of the subject. According to Machen, [60] "He observed the fact that property belonged in law to a corporation and not to any individual, and the question he put to himself was, 'who or what is the real

[57] Corporations, 14.
[58] 2 Com. 458.
[59] 1 Wilgus, Corporation Cases, 157, *et seq.*
[60] Machen, Corporate Personality, Harvard Law Review, Vol. XXIV, No. 4, Feb., 1914, p. 255.

owner of this property?' * * * Savigny's answer was that the corporate property belonged to a fictitious being and not to any real person or entity. He took as his starting point the proposition that ownership involves the possession of a will by the owner; and he concluded that inasmuch as a corporation does not really possess a will, it must as a property owner be a fictitious person. At the same time, as an acute French writer has demonstrated, Savigny and his followers, paradoxical as it may seem, impute a certain reality to this fictitious person."[61] In Savigny's doctrine may be recognized the most prominent features of the orthodox common law theory of Anglo-American law.

The Realistic Conception. Another theory, which we may speak of as the third in our discussion, grew up side by side with Savigny's Juristic Person concept. It developed among German jurists who became convinced that the corporate entity, whether a person or not, was not a fictitious being, but a reality. The real nature of the thing in itself apart from its status in law received emphatic approval. It was held that corporate personality is neither fictitious, nor artificial, nor created by the state, but both real and natural, recognized but not created by law. Gierke was the leading exponent of this school.[62] It has long held sway in Germany. The more radical adherents to the view develop the analogy of this corporate being—this real person,—to an organism, and describe it as possessing organs like human beings. They endow it with a will and with senses. But Gierke and the more moderate realists take a less anthropomorphic view of the creature and subject their theory to a critical analysis based on common sense and the non-human nature of the corporate person. They claim, however, that the real entity comes into existence when the group comes into existence, and it does not depend upon the

[61] Citing De Vareilles-Sommières, Les Personnes Morales, Chapter 11.
[62] Otto Gierke, Political Theories of the Middle Age, translated with introduction by Maitland.

law to create it even though its legal status must necessarily be determined by law.

The Anglo-American Fiction Theory. A fourth theory of the nature of the corporation combines those to which I have already referred. It is the outgrowth of the courts' application of theories to practical cases. It effects a compromise between the Juristic Person theory and the Realist conception in order to evolve a practical working theory based on experience and common sense. The reality of the group entity is either denied or strictly limited and its origin and existence is made to depend upon the express will of the state. Even the act of the state in granting permission to individuals to associate together for a specified purpose with certain accompanying privileges or immunities, monopolies or special rights, is not conceived of as necessarily endowing the corporate entity with reality distinct from the individuals associated together. But the law finds it necessary in the interest of justice, for the protection of the rights of those who deal with the corporation, to treat the group as if there were an entity distinct from the individuals in the group, and capable of acting as such. That is, the law raises up the "fiction" of corporate existence. While jealously denying that the charter act has given birth to a new being or entity, it grants to certain individuals associated together the right, franchise, or privilege to do certain acts and pursue certain objects as a unit. And, the courts have held, that for convenience' sake, to facilitate the administration of justice in the interests of the public, they will deal with the corporate group as though it really were what, they say, it is not—a real entity, sometimes described as a person, distinct, separate, and apart from the individuals that compose it. This, then, is the American "fiction of corporate existence." It will be seen, however, from the discussion of cases in the following chapter, that the courts tend to abandon the fiction and accept the truth that the corporate entity is real, separate and distinct from the individuals that compose it.

The question may well be raised at this point: What is meant today by the fiction of corporate existence? That the courts treat the corporate entity as having undoubted reality and say equally positively that this conception is well known to be founded on a fiction, is necessarily the source of great confusion. If the doctrines of Coke and Blackstone as followed by Marshall and Story are still the law, then not only the separate existence, but the fact of existence of a corporate entity is merely a fiction of the law. But fictions, as judicial doctrines, change imperceptibly from time to time. Whether or not it be contended that Marshall's theory is actually accepted today, the fact cannot be doubted that our present-day doctrine had its origin and source in the Juristic or Artificial Person concept and that the language of the courts still infers their acceptance of the entire theory as a legal fiction.

A study of the cases, however, and the actual facts involved, suggests the conclusion that the probable source of much of this confusion is the fact that there seems seldom to have been made any distinction between the idea of the corporate entity as such and that entity referred to as an artificial or juristic "person." The latter term is used interchangeably with the former in most of the early definitions, sometimes as merely descriptive and sometimes as a substitute for the term "entity." It is clear, that the artificial-person theory of Coke and Blackstone centered about an entity which was regarded as a person, and therein lay the heart of the fiction of corporate existence in their day. This was the conception still in the mind of the court in the Dartmouth College case in 1819. It was natural to personify the spirit of an ecclesiastical or eleemosynary institution. But when the private industrial and business corporation came into the foreground in the nineteenth century it cannot be said that the immortal "spirit" of the institution was often in the minds either of the incorporators or the courts or anyone else who dealt with it. What did become of great significance, however, was the part of the fiction which described the corporate entity as separate and distinct from the individual members of the

group. And it is this new emphasis upon an aspect of the fiction concept, earlier subordinated to the personal idea, which has raised such vital issues of policy and law in American courts. It is a matter of indifference to those who adhere to this later interpretation, as the essence of the fiction doctrine, whether the entity be described as any sort of a person or not, so long as that part of the theory is preserved which, they say, absolutely divorces the separate and distinct corporate entity from its individual members and grants it in law an independent existence apart from the incorporators.

This, however, pushes the idea of separate existence to the point of absurdity in a total disregard of facts and common sense. It ignores the relation which always necessarily obtains between the individual will and the group will. It accepts the court at its word, assumes the corporate entity to be a fiction and draws a not illogical conclusion from the language usually adopted to describe it. In fact, champions of this idea ride the corporate fiction to death, and call down upon themselves reproval in the reminder that "it is a certain rule that a fiction of law shall never be contradicted so as to defeat the end for which it was evoked, but for every other purpose it may be contradicted."[63]

Somewhere, then, between the divorced-entity concept, which the courts will neither accept in fact nor in theory, and the concept of the corporation as a real entity sometimes described as a juristic person, which the courts accept in theory as fiction but in fact as real, we must look for our theory of today. That part of the fiction theory that treats the separate entity as real, is identical in language with the Realists' conception. Hence the difficulty of knowing whether, as a matter of fact, the courts are acting upon the Realist or the Fiction Theory when they proceed along this line of reasoning. Precedents, and the language of the courts, necessarily interpret their view as in harmony with the fiction theory which is the heritage of law as

[63] State v. Standard Oil Company, 49 Ohio State, 137 (1890).

a system. This is necessary because of the nature of systematized legal reasoning based on logical juristic concepts. But legal writers and students of jurisprudence are not required to be bound by a static legal system, and are inclined more and more to go behind the professed tents of judicial reasoning and view the method of treatment of facts and the actual points decided, from them deducing a truer juristic concept, free from the bonds of *stare decisis*. Their conclusion must be that the corporate entity does exist as a reality and is no fiction.

The reasonableness of this conception is apparent in that the doctrines of agency, notice, and estoppel are quite as applicable to the corporate entity as to the individual. They do, however, postulate a will, and this brings up the question of the relation of will to personality, and of the place of the concept of personality in the new doctrine of the real corporate entity. If the entity can exert a will to appoint an agent, can it commit a crime? Before taking up this point, it may lend clearness to the preceding analysis of the fiction theory to discuss a typical case involving it.

State v. Standard Oil Company. In the case of State v. Standard Oil Company,[64] the Supreme Court of Ohio said: "That a corporation is a legal entity apart from the natural persons who compose it, is a mere fiction, introduced for its convenience in the transaction of its business, and of those who do business with it; but, like every other fiction of the law, when urged to an intent not within reason and policy, may be disregarded." Justice Minshall, in stating what he conceived to be the proper theory as regards the nature of the corporate entity, perceived "no reason why the principles applicable to fictions in general could not apply to the fiction that a corporation is a personal entity, separate from the natural persons who compose it, and for whose benefit it has been invented."

[64] 49 Ohio St. 137, 30 N. E. 279, 287.

In Justice Minshall's statement there is danger of a confusion of ideas as to the exact nature of the fiction involved in corporate existence. Upon an examination of his opinion we find that what was really decided was not that the existence of a corporate entity is a fiction, although he asserts this to be the fact. Nor, that its existence separate and apart from the stockholders in the sense of its having distinct rights and liabilities, is a fiction, although the language used also makes that assertion. The point actually decided was: "the idea that a corporation may be a separate entity, in the sense that it can act independently of the natural persons composing it, or abstain from acting where it is their will that it shall, has no foundation in reason or authority, is contrary to fact, and to base an argument upon it when the question is as to whether a certain act was the act of the corporation or of its stockholders, cannot be decisive of the question, and is therefore illogical; for it may as likely lead to a false as to a true result." The court denied, therefore, the claim of the defendant that because the corporation is a legal entity, separate from its stockholders, it can only be affected by such acts and agreements as are done or executed on its behalf by its corporate agencies, acting within the legitimate scope of their powers. For, as Justice Minshall pointed out, the defendant did not deny the averment of the petition that all of the owners and holders of its capital stock, including all the officers and directors of the corporation, signed the agreements in question. And the court's decision held that where all, or a majority of the stockholders composing the corporation do an act which is designed to affect the property and business of the company, and which does affect it in the same manner as if there had been a corporate act based on a formal resolution of the Board of Directors, the act should be regarded as that of the corporation. And, since it would have been *ultra vires* and against public policy as a corporate act, it could not stand before the law. It was done, said the court, by the individual members of the corporation in their individual capacities, but

for the purpose of concealing their real object. To prevent such an abuse of corporate power, the act might be challenged as a corporate act by the state in a proceeding in *quo warranto* against the corporation. The reason which the court gave for thus disregarding the theory of the separate corporate entity was the control which a corporation is given in fact, through its members, over the selection and conduct of the corporate agencies,—in this case a holding company.

Thus, an agreement by which all, or a majority of the stockholders of a corpartion transferred their stocks to certain trustees, in consideration of the agreement of the stockholders of other corporations and of the members of limited partnerships, engaged in the same business, to do likewise, was held to be the act of the corporation. In exchange for such transfer, each individual was to receive, in lieu of his stocks and interests, trust certificates to be issued by the trustees, equal at par to the par value of his stocks or interests. By the agreement the trustees were empowered, as apparent owners of the stock, to elect directors of the several corporations, and thereby control their affairs in the interests of the trust so created. They were to receive all dividends made by the several companies and from this common fund were to disburse dividends to the holders of the trust certificates. This arrangement, said the court, tends to the organization of monopolies to control production as well as prices, and is against public policy.

It seems clear, then, that Justice Minshall's statement is not to be taken as broadly as the words imply when he says, "the general proposition that a corporation is to be regarded as a legal entity existing separate and apart from the natural persons composing it, is not disputed, but that the statement is a mere fiction, existing only in idea, is well understood, and not controverted by anyone who pretends to an accurate knowledge on the subject." As stated above, it is hardly to be doubted that what was in Chief Justice Marshall's mind when he set down his definition of a corporation in the Dartmouth College

case[65] was Blackstone's definition referred to in Justice Story's concurring opinion, and stated as follows: "An aggregate corporation at common law is a collection of individuals united into one collective body, under a special name, and possessing certain immunities, privileges, and capacities in its collective character, which do not belong to the natural persons composing it. Among other things it possesses the capacity of perpetual succession, and of acting by the collected vote or will of its members, and of suing and being sued in all things touching its corporate rights and duties. It is, in these, an artificial person, existing in contemplation of law, endowed with certain powers and franchises which, though they must be exercised through the medium of its natural members, are yet considered as subsisting in the corporation itself, as distinctly as if it were a real personage."[66]

This definition clearly introduces the Juristic Person theory that Coke and Savigny espoused. But later decisions of the United States Supreme Court do not bear out the statement of the Ohio court that the corporate entity itself is a fiction. For instance, in Hale v. Henkel,[67] Mr. Justice Brown, speaking for the court, said: "A corporation is, after all, but an association of individuals under an assumed name and with a distinct legal entity." There is no hesitation here in according reality to the distinct legal entity.

In Mr. Justice Minshall's opinion in the Standard Oil Company case, the same confusing inference as to a necessary connection between the entity and a fictitious person appears, as in the definitions of Blackstone, Marshall, and Story. It is not necessary, as Justice Minshall seems to infer, to assert that every theory of the existence of a distinct corporate entity is a

[65] "An artificial being, invisible, intangible, and existing only in contemplation of law,—a mere creature of the law,—possessing only those powers which the charter of its organization confers upon it, either expressly, or as incidental to its very existence."

[66] 1 Blackstone Commentaries, 469, 475; 1 Kyd, Corporations, 13, 69, 89; 1 Woodes, 471, etc.

[67] 201 U. S. 43, 76.

fiction simply because the doctrine of a personal entity was recognized as fiction. And so, when he says that "no reason is perceived why the principles applicable to fictions in general should not apply to the fiction that a corporation is a personal entity, separate from the natural persons who compose it, and for whose benefit it has been invented," his inference does not necessarily follow that because the existence of a corporate "person" is a fiction, therefore every view of the existence of the corporate entity must be a fiction.

The Nature of Legal Fictions. The question might well be raised at this point: What is a fiction? Or rather, since it is legal concepts with which we are here dealing, what are fictions of law? We find an answer ready at hand. Professor Gray, in his "Nature and Sources of Law," tells us that fictions are devices adopted by the courts for the purpose of doing justice. Ihering, he says, divided them into two classes: historic and dogmatic fictions.[68] Historic fictions are devices for adding new law to old without changing the form of the old law. Such fictions have had their field of operation largely in the domain of procedure, and have consisted in pretending that a person or thing was other than that which he or it was in truth (or that an event had occurred which had not in fact occurred) for the purpose of thereby giving an action at law to or against a person who did not clearly come within the class to or against which the old action was confined.

The prætors, as Professor Gray points out, employed such a fiction in aiding them to build up the towering fabric of the Roman law on the narrow basis of the Twelve Tables. "Thus, persons to whom the prætor thought it just that a man's property should go on his death,—relations, for instance, on the mother's side, who were not heirs,—were, by a fiction, considered heirs and were allowed to use an action such as heirs

[68] 3 Geist d. om. R. (4th ed.), sec. 58, pp. 301-308. J. C. Gray, Nature and Sources of Law, sec. 74.

could use. *Heredes quidem non sunt, sed heredis loco constituuntur beneficio prætoris. Ideoque seu ipsi agant, seu cum his agatur, ficticiis actionibus opus est in quibus heredes esse finguntur.*"[69]

"So when it was thought just that an action which was given by the Civil Law only to or against a Roman citizen, should be extended to or against a foreigner; *Civitas Romana peregrino fingitur, si eo nomine agat aut cum eo agatur, quo nomine nostris legibus actio constituta est, si modo justum sit, eam actionen etiam ad peregrinum extendi.*"[70]

Fictions have played an important part in the administration of the law in England. It is said to be "characteristic of the two peoples, the Roman and English, that the use of fictions in England was bolder and, if one may say so, more brutal in England than it was in Rome. * * * One of the purposes for which English courts allowed fiction was to extend their jurisdiction. * * * For instance, of the three Superior Courts of Law, The King's Bench, the Common Pleas, and the Exchequer, the Court of Common Pleas alone had original jurisdiction of causes between subject and subject not involving violence or fraud; but, as an exception, when a man was in custody of the Marshal or prison-keeper of the Court of the King's Bench, he could be sued also in the latter court. Now a plaintiff wishing to sue in the King's Bench for ordinary debt would allege that the defendant was in the custody of the Marshal, and that therefore the case was within the jurisdiction of that court. The allegation was false, but the court did not allow the defendant to contradict it."

As Maine says, in his "Ancient Law,"[71] "fictions of the jurisdictional kind are almost a necessity of the law at a certain stage of human development. They satisfy the desire for improvement, which is not quite wanting, at the same time that

[69] Ulp. Fragm. 28, 12, quoted in Gray, Nature and Sources of Law, sec. 74 ff.

[70] Ulp. Fragm. 28, 12, quoted in Gray, ibid.

[71] Sir Henry Maine, Ancient Law (5th ed.), 26.

they do not offend the superstitious disrelish for change which is always present. But as a system of law becomes more perfect, and its development is carried on by more scientific methods, the creation of such fictions ceases, and better definitions and rules are laid down which enable us to dispense with the historic fictions which have been already created." Such fictions, it has well been said, are like scaffolding,—useful, almost necessary, in construction—but, after the building is erected, serving only to obscure it. A chief objection to their continuance, to quote again from Maine,[72] is that "they are the greatest of obstacles to symmetrical classification. There is at once a difficulty in knowing whether the rule which is actually operative should be classed in its true or in its apparent place." No more strikingly is this truth illustrated than in the fiction of corporate existence. This, however, is more properly classified with Ihering's second class of fictions, the dogmatic.

Dogmatic fictions, says Professor Gray, instead of being obstacles to symmetrical classification, have been introduced and used as aids to it. These dogmatic fictions are not employed to bring in new law under cover of the old, as are the historic fictions, but to arrange recognized and established doctrines under the most convenient form. Thus, the doctrine of constructive notice, as in the case of a recorded deed, is applied as a fiction by which a subsequent grantee from the original grantor is treated as though he had knowledge of the first deed. Likewise, in corporation law this doctrine of constructive notice is applied to third persons dealing with the corporation, with the result that they are treated as having knowledge of the charter and hence are presumed to know whether an act of the corporation is *ultra vires,* or an act of an officer is beyond his powers, and they may be barred, therefore, from recovery on a contract unperformed on the part of the corporation, although they may have performed their obligation in good faith and with no

[72] Sir Henry Maine, Ancient Law (5th ed.), 26, 27, 28.

actual knowledge that the contractual agreement was *ultra vires* as to the corporation.

I have already referred to the doctrine of the courts that the "law does not resort to fictions without a motive, or for any other purpose than a compliance with the requirements of justice."[73] "All fictions of law have been introduced for the purpose of convenience and to subserve the ends of justice."[74] It is in this sense that the maxim, *"in fictiones juris subsistit æquitas,"* is used and the doctrine of fictions applied. But when fictions are used to an intent and purpose not within the reason and policy of the fiction, they have always been disregarded, say the courts.[75] As Lord Mansfield, Chief Justice, said, "It is a certain rule that a fiction of law shall never be contradicted so as to defeat the end for which it was enacted, but for every other purpose it may be contradicted."[76] And Justice Minshall, in the Standard Oil Company case, says, that the Anglo-American fiction of corporate existence has been introduced for the convenience of the corporation in making contracts and acquiring property for corporate purposes, in suing and being sued, and to preserve the limited liability of the stockholders by distinguishing between the corporate debts and property of the company and of the stockholders in their capacity as individuals. It is, he says, harmless and convenient so long as it is properly used; but where it is urged to an end subversive of its policy, the fiction must be ignored and the question determined whether an act done by shareholders, that is to say, by the persons uniting in one body, was done simply as individuals, and with respect to their individual interests, or was done ostensibly as such, but as a matter of fact, to control the corporation, and effect the transaction of its business, in the same manner as if the act had been clothed with all the formalities of the corporate act.

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[73] Smith v. Furbish, 68 N. H. 128.
[74] State v. Standard Oil Company, 49 Oh. St. 137.
[75] Broom, Legal Maxims, 130.
[76] Johnson v. Smith, 2 Barrows, 962.

Legal writers are not always in accord with the positive statements of the courts as to the value of the corporate fiction. It is true, as Professor Gray points out, that dogmatic fictions help to arrange and classify the law.[77] But they are an aid only if one is always ready to recognize that fictions are fictions, and be prepared to state the real doctrine for which they stand. Wherefore, since the fiction of corporate existence is evidently a dogmatic fiction, it should, therefore, be used only for its usefulness as an aid to the classification of the law and an understanding of the historical evolution of the corporate entity. Beyond that, however, it should not be set up as an objective reality. The real nature of the corporate entity should be recognized today whenever it is associated with the fiction. Failure to realize this often leads to the conclusion that Geldart suggests, that, while "an historic fiction may be misleading and cumbrous, it is at least perfectly evident and serves a useful purpose, while the dogmatic fiction is obscure and serves no useful purpose whatever but to darken counsel."[78]

A somewhat more elaborate discussion of the historical fiction may indicate the distinction between it and the dogmatic type. An historical fiction, to repeat, is one which has been used for the creation of new rights or new remedies, where the existing law has insufficiently provided for the protection of interests which a later age thinks deserving of protection, but does not venture to protect by an open alteration of the law. Thus, when the archaic procedure which protected a freeholder in our law had become too cumbrous to accord adequate protection, while the leaseholder's interest was protected by newer and more workable machinery, the former was allowed to share in the benefits of the new invention by setting up a fictitious leaseholder in whose name proceedings were taken, and whose existence the defendant was forbidden to deny. In such a case we

[77] Gray, Nature and Sources of Law, p. 48, 36.

[78] W. M. Geldart, Legal Personality, an inaugural lecture delivered before the University of Oxford at All Souls College, November 5, 1910; Law Quarterly Review, Vol. XXVII, p. 96, January, 1911.

have a genuine and indisputable fiction: John Doe, in truth, exists only on paper, a dummy whose strings are pulled behind the scenes by the true owner. No one had any difficulty in seeing through the fiction, or in pointing to the real plaintiff behind the fictitious one.

Legal Fictions Applied to the Corporation. The corporate entity, however, is not such a fiction as John Doe was. The entity did not spring into existence for the first time at the call of the court, as did John Doe. Corporate bodies existed and were recognized before a theory was invented to explain their existence and recognition. It is clear that no historic fiction preceded the existence and legal recognition of such bodies. The corporate name by which a body can contract and hold property, can sue and be sued, is not a John Doe put forward by recognized and well defined persons who for some reason need a disguise. If there is a fiction involved, it is of the other kind, the so-called dogmatic fiction.

The dogmatic fiction of corporate existence consists in conceiving an abstraction, attributing to it the will of a being, and regarding it as a person. Now it is not the abstraction that is unreal. Reality does not merely connote that which is concrete and tangible. A right is real. An abstraction may be real. But the fiction consists in calling the abstract entity a human being. That is what has usually been meant by the term fictitious, or artificial. But "juristic" does not necessarily connote all that "fictitious" implies. It is a dogmatic fiction to speak of a corporation as a fictitious person, and when the term "juristic" is used in place of fictitious in connection with the word "person" it is plain that the two are meant to be used interchangeably. But it is not necessary so to use them. The corporation is not, like John Doe, no thing at all. A corporation actually is an organized body of men, to which the state has given powers to protect its interests, and the wills which put these powers in motion are the wills of certain men in their corporate capacity, determined on the basis of representation

according to the plan of organization of the corporate body. Now, the powers granted by the state are not the rights of the individual men in the group, for it is not the interests of those individual men that are protected. Therefore, since the corporate entity has rights, says the dogmatic fiction, it must be able to exert a will, and since will is the product of the human mind, let the corporation be spoken of, for the purpose of clarity in organizing our legal thinking, as a person.

One interpretation of this fiction, therefore, is the deduction that since only a human being can exercise will, the corporate entity must be regarded as a human being. Since it is not one in fact, it is, therefore, a fictitious person. Another interpretation goes a step further back. It concludes that the entity itself is unreal—that is, that the entity itself does not exist, but must be regarded as existing to support the rights the law confers upon it. Hence it must be regarded also as exerting a will; and since it has, likewise, no will in fact, the fiction must attribute to the corporation the wills of the individual members that compose it. This orderly arrangement of the law, however, certainly has sacrificed something of facts. It may well be asked, how, if only a human being can exercise will, and if will is the product only of the human mind, can it be possible to say that the corporate entity, which is not human, exercises a will of its own?

In the first place, looking at the facts, it must be conceded that there is a real entity arising from an organized group. Whether the entity is claimed to be concrete, as it is claimed that an army is a concrete object visible to the senses, or an abstraction,—in either case it is real. In the second place, the entity does exert a will of its own distinct from the will of any one individual in the group, although influenced by all. There is nothing contradictory in this conception. Neither the will itself, nor its sources, are tangible and concrete in their reality even in the human being. The individual human will is made up of a complex of ideas finally mastered by one which is said

to be dominant at the moment the will translates itself into action. The source of constituent ideas and the ideas themselves are as often unconscious as conscious. The mind is the conduit through which they pass and in which they are organized. A similar process takes place in the formation of the group will. Conflicting ideas struggle for supremacy and finally focus upon a particular object. They are organized under a dominant idea most suitable to attain an end, and the group will is then translated into action by the will of designated officers or agents who act for the corporation. In the individual, the same mind is the conduit and the organizer and the initiating force that acts upon the ideas which make up the will. Wherefore the will is said to be that of the individual. In the corporation the individual mind of the agent is subjected to the limitation that requires him to reject all ideas known to be in conflict with the group interests. He is not free, in making up his mind, to guide his choice of ideas that would otherwise be given equal chance to predominate, by his own interests, but must subject them to the test of subservience to the group interests to which the law has granted rights and duties for protection.

Wherefore, it cannot be rightly said that "with all legal persons, except normal human beings, there is a fiction of attributing the will of a man to some one or thing other than himself," nor that "it matters not how or what that someone or something else is," nor that "the step is as hard to take and no harder whether he, she, or it be an idiot, a youth under legal age, a horse, a steam tug, or a corporation."[79] It may be true enough that neither the idiot, the horse, nor the steam tug has a real will. But it is certainly not true that a state or a corporation has none. Hence, so long as the corporate entity is treated as a reality, there is no occasion for any longer regarding as fiction the formation of an abstract entity, nor is it necessary to attribute to the corporate entity the wills of each member in

[79] Gray, Nature and Sources of Law, p. 48.

the group as such, on the postulate that there can be no other than individual human wills. If Mr. Gray's reasoning be followed, then all representative action rests upon fiction,—a conclusion which certainly cannot aid us in understanding the real meaning of the doctrine of representation.

The earlier view of the corporation under the fiction theory involves a double fiction. By the first part, the entity itself is said to be created; by the second part, the wills of the individual men are said to be attributed to it. We submit that neither fiction is necessary, useful, nor in accord with the facts. The entity is real, and not fictitious. Moreover, the representative corporate will is real. Hence it is improper and unnecessary to attribute the wills of the individuals as such to the entity in any other sense than that which regards them as the source of, or the materials out of which is constructed, the group will. However, even if the corporation be regarded as a real thing with a real will, yet it would be fiction to call it a person. The only reason why idiots and ships have not been called juristic persons, and classed with corporations, we are told, is that in the Roman Law and the Common Law the prevalent idea seems to have been that corporations were fictitious entities, were things only by fiction, and that, therefore, in their case, as distinct from the case of idiots and ships, there was need, according to the fiction theory, of a double fiction, and it was thought that they ought to be put under a different head and distinguished by a different name—that is, "juristic persons." Under the Roman Law, says Professor Gray, there was little discussion of the nature of corporations, and the Roman concept, therefore, is of primarily historic interest only. Under the Common Law, likewise, there has been little discussion. Such analysis was alien to the eminently practical character of both systems. And it is significant, therefore, that when Professor Gray wrote his book, in 1906, he made the statement that "the prevailing opinion has undoubtedly been that a corporation is not a real thing, but there cannot be said to be any settled

opinion to that effect." And Gray approached the subject from the point of view of scientific exposition rather than as one seeking converts.

Disregarding the Corporate Fiction. The question may now be considered as to how far, and to what extent the courts should disregard the corporate fiction? Courts of law cannot for practical reasons launch out upon a course based upon pure logical reasoning in disregard for precedent and established juristic concepts. But they can and should treat the corporate entity as a reality. They should go further, and accept the corollary that there is a difference between existence and legal acting capacity. They should drop the time-worn reiteration that the corporation is a mere creature of the law existing only in idea, when what is actually meant is that the legal status, legal powers, and legal acting capacity of the group have their source in law and, for the most part, depend upon a charter act of the state. I say, for the most part, because it is evident that in the case of *ultra vires* acts, torts, and crimes, the court is compelled to recognize the necessary limitation of their fiction inasmuch as the group does act without the law, beyond the corporate powers, and in contravention of statutes. Moreover, the use of the *de facto* doctrine of corporate existence and the application of estoppel to deny the existence of the corporation under many circumstances, in effect disregards the fiction. And when we here speak of "disregarding the fiction" of corporate existence, what we mean is "having regard for the reality" of the corporate entity. This, it must be noted, is directly opposite in meaning from "disregarding the separate entity." Hence, in the question so often put to the minds of students and legal writers, "How far and to what extent will the courts disregard the fiction of corporate existence and deal with the natural persons that compose the corporation?" there is an inherent contradiction. The question more properly stated would seem to be whether the real entity is

substituted for the fictitious one; or the real or fictitious entity is to be disregarded completely.

In language, the courts seldom do disregard their fiction. In fact, they do constantly disregard it. Just how far this is true will be discussed at length in the following chapter. There are, however, two notable classes of cases which may be profitably mentioned at this point. The one class includes the other. In the broader class,—that involving the status of foreign corporations—the limitations of the dogmatic fiction which restricts the corporate entity to the state of its creation, are set forth. In the other class of cases,—that dealing with the citizenship of corporations—the fiction of separate corporate existence has been set aside under what the court regards as exceptional circumstances; but an additional fiction has been added to overcome the difficulties which resulted from this action, with the result that there now exists in our law an irrebutable presumption that all of the members of a corporation are citizens of the state in which it has its origin. Curious situations have arisen from this doctrine. For instance, upon this theory of corporate citizenship,—the federal courts have entertained suit by a member of a corporate body against the corporation itself, on the ground of diversity of citizenship. As plaintiff, the individual member was a citizen of one state, whereas, by the irrebuttable presumption of corporate citizenship he was at the same time regarded as a citizen of another state, that of corporate origin.

This is a clear case in which the courts have treated the separate corporate entity as a reality and neutralized the effect of disregarding the fiction theory by the introduction of another fiction.

It may be said, finally, as to the Anglo-American fiction theory of corporate existence, that the theory should be examined, whenever used, to determine the particular interpretation sought to be placed upon it. If we look at the corporation as it exists today, it is not a fiction that it is an entity distinct in rights and duties from the individual persons that compose it.

If we overemphasize the "separate and distinct" quality, however, and give it such a meaning that we deduce a conclusion which denies any possible relation between the entity and the individual members that compose it, then it is truly fiction and a foolish one. If we regard it as a person and ascribe to it something more than impersonal existence as an entity—that is, personality—then it may be either a fiction or no fiction according to whether we adopt the language and theory of the anthropomorphic realists, and the conceptions of Coke, Blackstone, and Savigny, or choose to be guided by reality and define corporate personality in terms of those rights, duties, and attributes of will, which, from the nature of the entity, can belong to a corporation. One more conclusion is suggested: Heretofore, it has been the existing "juristic person" or "entity" which has been designated as the content of the fiction. The related contention that the creature exists only in contemplation of law and by act of the state, is not consistent with the adoption of the concept of reality, unless it be given a new meaning, such as "legal status and powers," or "legal capacity," as distinct from that "acting capacity" which is inherent in a group wherever men come together for a common purpose.

Corporate Personality. This has ever been a troublesome concept in theories of corporate life. As Deiser says, "the *persona ficta* will not be ignored. He is said to be a corporation, a collective person, a legal fiction, a convenient factor in legal reasoning, etc.; but real or fictitious, personal or impersonal, animate or inanimate, he emerges uncannily from every fiat of extinction, much after the fashion of Antæus who, cast to earth, renewed his vitality."[80]

What, then, is corporate personality? I have shown that the idea of "person" was the heart of the early fiction theories. If we cast aside the fiction of a person, and accept in its place the reality of an entity, what qualities of personality, if any, can

[80] G. F. Deiser, The Juristic Person, University of Pennsylvania Law Review, Vol. 48, N. S. 570, 1, No. 3, Dec., 1908.

be attributed to this real entity? Whether or not it is correct or useful to designate it as a person must depend upon whether the use of the term is merely descriptive, metaphorical, or based upon positive qualities which attach to a person as such. The early theories of the fictitious person proceeded upon the following basis of reasoning: All rights and duties attach to persons; there are, in the case of a corporation, definitely ascertainable rights and duties. Therefore, there must be a person. It must again, however, be noted that the idea of personality has been confused with that of reality. To assert the reality of the corporate entity does not, however, necessarily carry with it the assertion that the entity is a person, nor is it possible, on the other hand, to regard the entity as a wholly lifeless, bare, technical device devoid of initiative.

The doctrine which conceives of the corporation as merely an association of individuals has regarded the corporate entity as only an impersonal device to which group rights and duties are attached for convenience in treating with the group for purposes of administration of justice. This view would regard the entity as merely a conduit of individual rights and duties which assume a particular form for certain purposes. It has been pointed out that Savigny's Juristic Person was regarded as fictitious, and that the radical wing of the Realist School reacted to the other extreme by identifying the corporate person with an animal organism. The syllogism of the fiction school may be stated; as Henderson suggests, as follows: "Only persons can be subjects of rights and duties. A corporation is the subject of rights and duties. Therefore the law must set up the fiction that a corporation is a person. The realist doctrine states the major and minor premise in the same way, but its conclusion is that a corporation actually is a person. Now, if we deny the major premise, both the conclusions are rendered unnecessary, and the conflict between them becomes academic."[81]

[81] Henderson, The Position of Foreign Corporations in American Constitutional Law, p. 165, Harv. Studies, 1918.

Mr. Henderson states that "modern jurisprudence has very generally rejected the major premise, and suggests that the assumption, that a person alone can be the subject of rights, is based on the conception of a right as a philosophic entity, springing out of the nature of man independent of the law and anterior to it. Now this use of the word really identifies 'right' with 'interest.'[82] But this is not the sense in which the word 'right' is used when we speak of a corporation. When we speak of a corporation being the subject of rights, we mean that it has the capacity to enter into legal relations,—to make contracts, own property, bring suits. Rights, in this sense, are pure creatures of the law. They are part of the technique by which law expresses a result which it wishes to attain. In this sense," it is said, "anything can be made a legal unit and the subject of rights and duties,—a fund,[83] a building,[84] a child unborn,[85] a family."[86]

Now, if this definition of a right be accepted, the conclusion would be correct, that there is no reason, except the personal one, why, as someone has suggested, the law could not accord to the last rose of summer a legal right not to be plucked. The absurdity of this conclusion, however, is an admission that such a definition of a legal right is not a practical one. And the conclusion to which it leads, that the corporate entity is not a person at all, but merely an impersonal legal device for the practical convenience of the courts, is a logical but not an acceptable deduction from the premise. A more satisfying and equally practical view defines legal right as the power in the possessor "to make a person or persons do or refrain from doing a certain

[82] Roscoe Pound, Interests of Personality, 28 Harv. Law Review, 343, 345.

[83] A bank has recently been incorporated in Australia without incorporators. See Journal of the Society of Comparative Legislation, N. S. xvi, Pt. 1, 57.

[84] German "Stiftung".

[85] Lutterel's case, Precedents in Chancery, 50.

[86] Maine, Ancient Law, 197.

act or acts, so far as the power arises from society imposing a legal duty upon such person or persons."[87]

This conception of a right as being conditioned for its existence upon the concomitant presence of a power to exert initiative to enforce it, quite naturally leads to the conclusion that there must be a will to exert that initiative. Now, a corporation has the power to exert initiative to enforce its rights. What, then, it may be asked, is the nature of the will which sets in motion such action? It is not the will of any one individual in the group, yet it manifestly must be set in motion by someone in the group.

Representation and Group Will. Here we meet the doctrine of representation. Its presence in the concept of the nature of the corporation bears testimony to the closeness of the likeness of the concept of the nature of the corporation to that of the nature of the state. The idea of joint relation requires, in addition to identity of purpose, a connecting tie between a number of persons with reference to that purpose. For instance, in the case of the state, inasmuch as the public as a legally disconnected mass of individuals cannot control legal rights, the rights are exercised by the state through its government, and, in so far as enjoyment is concerned, by any individual who can assert an interest. In the case of a partnership, to take another example, unanimity of action is required by law. The absence of it dissolves the partnership. But this is impracticable in corporations or the state. Continuity of existence and control is one of the necessary objects to be attained. If the members of the group disagree, the law will accept the action of those who do concur as the action of all the associates, ignoring those who fail to act. And if all of the associates agree as to the action, but differ as to the method to be pursued, the law may indicate which of the contending parties shall prevail. In either case all are bound by a portion—that is, all of the associates act by representation.

[87] Gray, Nature and Sources of Law, sec. 48.

This, as Deiser points out, is original representation as distinguished from that which rests upon delegation such as agency, and which is common to the exercise of rights several as well as joint. Original representation assumes two forms according to the circumstances. Where some of the associates entitled to act abstain from action, those who act, a quorum, for example, are regarded as representing all. Where there is a difference of opinion the majority control the minority.

Where action by representation is recognized we may speak of the collective interest of a mere joint holding of rights. Where the number of associates is considerable the principle of representation becomes a practical necessity, and tends to assume a collective form of rights. In the case of governmental bodies, actual concurrence of all parties is imposible, and all direct action must be by original representation; likewise, the majority generally prevails. In the case of a business corporation of small membership, the acts of delegation are generally unanimous and everyone is likely to share in the joint control. Since representative action is possible, however, undivided control is likewise possible, and the collective body consequently acts and appears as a unity. The fact that persons who dissent are bound by the action of a majority does not mean that they are excluded from the act of representation. Their act of opposition means that they are given a part in influencing the formation of the controlling will by the assertion of their wishes and opinions; their failure to control indicates weakness either of position or of numbers. Abstention of action means acquiescence in the action of those who have actually taken part. A share in the control is legally secured to all, although that exercised by any one individual may prove incapable of affecting the final act.

The individual incorporator acts in several capacities. He may act as a member of a corporate group, in which case he exercises certain definite rights, or he may act as an individual, in which case the rights he can exercise are entirely different. "This difference in the nexus of a man's activities is recognized

in the principle described as 'subjective differentiation,'" says Deiser.[88] "The personal location or inherence of the corporate rights of an individual member of a corporation are determined by the relation of the individual to the corporation by virtue of his holding a share or stock of the corporation. It is designated objective determination." This impersonal determination of the location of corporate rights in individual members seems to subject the person to the objective right. And if this point of view be placed in the foreground, on the assumption that corporations are essentially property-holding bodies in which the control of the property and interest in it are separate, it is not illogical to come to the conclusion that each shareholder, being the owner of a qualified right, the association must be conceived of as the sum of the rights so qualified. This, however, seems to be looking at the mechanism of the corporation from one point of view only, and that the least important.

It will be readily conceded that the physical activity of a corporation is produced by the mental activity of the associates. The decision of the stockholders acting as a unit is not the distinct act of any individual. It is the resultant of desires never entirely harmonious, but fused together by discussion and compromise. This collective consciousness may be considered as the personality of the corporation. If we view the corporation from without, rather than from within, we must come to the conclusion that there is manifest a group will, an intent, a purpose, a determination, a deliberation, and, by implication of law at least, even malice. This point of view brings us back to the conception of the reality of the general will.

The will of the state is scarcely ever denied reality, even though views of its origin and source differ. Hobbes, for example, insisted that sovereignty must lie in a will, and that this will must be real and must be taken as representing or standing for the will of the community. "This," he says, "is more than consent or concord; it is a real unity of them all in one and

[88] The Juristic Person, University of Pennsylvania Law Review, January, 1909.

the same person."[89] To be sure, he treated the "moral person" (that is, the "juristic person") as a fiction. But so far from abandoning for that reason all idea of actual effective unity, he replaced the fictitious or abstract unity of a person by the "real unity" of an actual human being or a determinate group of human beings, to be taken as a unity of the commonwealth as such.[90] Locke felt that actual government is a trust, and that the ultimate supreme power remains in the community as a whole. "The difficulty in his case," as Bosanquet says, "is to understand how the will or interest of the community as such obtains determinate expression. Generally, and apart from particular cases of dissent, it is to be taken as one with the will of the governing body to which, according to the constitution, the work of government is given in trust. For Hobbes, political unity lies in a will which is actual, but not general; while for Locke it lies in a will which is general but not actual. Rousseau's General Will was expressed as the will of the whole society as such, or the wills of all individuals in so far as they aim at the common good. It is the assumed identity between the particular wills of the associated persons in a body politic which makes it possible for Rousseau to say that in all social co-operation the individual is obeying himself. This postulates a will which in some sense transcends the individual whose will it is, and is directed upon an object of wider concern."[91]

The definition of the state from the point of view of analytical political philosophy is postulated upon the presence of a

[89] Hobbes, Leviathan, Pt. II, Chap. xvii.

[90] Bernard Bosanquet, The Philosophical Theory of the State, pp. 104 ff.

[91] Bosanquet, Philosophical Theory of the State, pp. 104 ff.

Rousseau, Contrat Social, II, IV; and Bk. II, ch. III, in which Rousseau discusses the nature of the General Will as follows: "There is often a great difference between the will of all and the general will; the latter looks only to the common interest; the former looks to private interest, and is nothing but the sum of individual wills; but take away from these same wills the plus, and minus, that cancel one another, and their remains, as the sum of the differences, the general will." "Sovereignty is only the exercise of the general will."

sovereign will. Dr. Willoughby states it as follows: "The point from which the analytical political philosopher starts is that a politically organized group of individuals may be conceived of as constituting an essential unity, and that the entity thus created may be regarded as a person in the legal sense of the word; that is, as a being, existing in idea, possessing legal rights and obligations, as distinguished from those of the individuals who, concretely viewed, make up its body politic, and that, as such a personality, it is, through organs of its own creation, capable of formulating and uttering a legal will with reference to matters within the jurisdiction conceded to it. Regarded as a legal person, the prime characteristic of the state is that there is posited of it a will that is legally supreme * * * . The supreme legally legitimizing will is termed sovereignty."[92]

These theories of the state have been referred to since it is evident, on the one hand, that students of Political Science, Jurisprudence, and Philosophy of Law are far in advance of the legal writers and the courts in the unanimity with which they accord a real and distinct will to the group. On the other hand, it is evident that their concept of the state is taken from and built upon the legal concepts of corporate personality. And, in turn, legal writers on corporate personality regard the state as "the highest type of juristic person, because of certain distinctive marks which make it superior to all persons real or artificial."[93] And, as Dr. Willoughby points out, when regarded as a legal person the prime characteristic of the state is that there is posited of it a will that is legally supreme. Now, it is submitted that a group will is no more essential to the state than to the corporation as such. To be sure, the will of no other corporation than the state can be said to have the attribute of sovereignty, but that does not of itself lessen the essentiality of the common will to the group, sovereign or not sovereign. In

[92] W. W. Willoughby, The Juristic Conception of the State, American Political Science Review, Vol. XII, No. 2, May, 1918.
[93] Deiser, The Juristic Person, University of Pennsylvania Law Review, January, 1909, p. 310.

fact, if common objective, experience, and interests be the necessary substratum of the existence of a group will, the smaller the group, perhaps, the more certain will appear this constant community of joint interests and experience.

If we turn from the analogy of the will of the state to an analysis of the psychological concept of the individual human will, we arrive at a similar conclusion as to the reality of the corporate will. Bosanquet, in his discussion of the reality of the general will,[94] describes the individual will of a human mind as "a machine, of which the parts are ideas or groups of ideas, all tending to pass into action but liable to be counteracted, or, again, to be reinforced by each other. The groups of ideas are connected with each other by associations of all degrees of intimacy, but each is for the most part capable of being awakened into action by the appropriate stimulus without awakening more remotely associated groups, and the will, for the time being, consists of those ideas which are guiding attention and action. The ideas are not thrown together anyhow, but are more or less organized; some being of a nature which enables them to serve as a clue or plan in which others find their places; and in a sense every group of ideas might be called a single idea, and all that there is in the mind as the creator of a single idea,—that is to say, all its parts are connected in various degrees, and more or less subordinated to some dominant ideas which, as a rule, dictate the place and importance of the others. We know what a ruling idea is: it is one that has gained control of the mind and subordinated all the other ideas to itself. This mental system, with its dominant ideas in relation to external action, is the individual will."

Now, at first sight, says Bosanquet, "all of these individual wills, or minds in action, are separate machines locked up in separate boxes, each with its indicator outside, and the response which each of them will make to a stimulus from without is

[94] Bosanquet, Realty of the General Will, International Journal of Ethics, Vol. 4, p. 311, April, 1894.

determined by its own structure, which is again determined by its own private history. If we go no further than this we seem not to get any hint of a general will, but only a sum of individual wills, which need not have any reference to each other's ideas. It is true that the quality that makes certain ideas dominant in one individual mind does not necessarily insure their being dominant in other individual minds. But under certain conditions they will be. These conditions are, in brief, community of life and experience." Now certainly there is abundance of community of interests in the corporate group. That is the occasion and motive of incorporation. It is clear, then, that there is a real general corporate will, first, because the very motives which lead to incorporation have their roots in the common interests which form the substratum of a general will, and, secondly, because like the state, the very life of the group depends upon the exercise of the group will.

In the first part of this discussion group will was approached from the point of view of the influence exerted upon it by the individual members of the group. The analogy of the exercise of the will of the state is again useful here. It is not every member that can exercise the will of the corporation any more than in the case of the will of the state. Even where it is granted that those who assume to possess the right to exercise the general will do have the power, yet they have it only for certain purposes and must exercise it in the manner prescribed by law. In the case of the corporation, the charter is the enabling act and its fundamental law. In the case of the state it is the Constitution. In the case of the corporation it is the board of directors and officers and duly appointed agents; in the case of the state it is the government acting through executive, administrative, legislative, and judicial officers. An act of a corporate body or its agent which is beyond the scope of its charter powers, is said to be *ultra vires*. An act of the state by its legislature, if beyond the scope of the powers set forth in the constitution, is void. Moreover, just as it is said that the corporation must act through its regularly designated

agents in the form prescribed by its charter and by-laws, so the individual members of the state, in order to take part in the general will, must do so in a representative capacity.

In no case is this analogy more strikingly borne out than in the case of Luther v. Borden.[95] That case rose out of Dorr's Rebellion. "Borden, acting under the authority of Rhode Island, had broken into the house of Luther, who was at the time engaged in an attempt to establish the new government provided for by the constitution that had been adopted in a popular, extra-constitutional manner. Upon being sued in trespass by Luther, Borden justified himself by the plea that he was acting under the authority of the legal government of the state. Luther, upon his side, denied the *de jure* character of that government, and, therefore, its legal competence to empower Borden to exercise the authority he had exercised."[96] The decision of this point would have been in effect a decision of the means by which a state, in American law, can exercise its will. The argument is therefore of sufficient importance to warrant a somewhat more extended discussion of the case.

Upon behalf of Luther, as Dr. Willoughby points out, it was argued that "by the fundamental principle of government of the sovereignty of the people acknowledged and acted upon in the United States, and the several states thereof, at least ever since th Declaration of Independence in 1776, the Constitution and frame of government prepared, adopted, and established as above set forth, was, and became thereby, the supreme fundamental law of Rhode Island, and was in full force and effect, as such, when the trespass alleged in the plaintiff's writ was committed by the defendants. That this conclusion also follows from one of the foregoing fundamental principles of the American system of government, which is, that government is instituted by the people, for the benefit and protection and security of the people, nation, and community. And that when any govern-

[95] 7 How. (U. S.), 48 (1846).
[96] W. W. Willoughby, Constitutional Law, Vol. I, sec. 79.

ment shall be found inadequate or contrary, to these purposes, a majority of the community hath an indubitable, inalienable right to reform, alter, and abolish the same, in such manner as shall be judged most conducive to the public weal."

In support of this position it was argued that the sovereignty of the people is supreme, and they may act in forming a government without the assent of the existing government; that the people are sole judges of the form of government best calculated to promote their safety and happiness; that, as the sovereign power, they have the right to adopt such form of government; that the right to adopt necessarily includes the right to abolish, to reform, and to alter any existing form of government, and to substitute in its stead any other that they may judge better adapted to the purposes intended; that if such a right exists at all, it exists in the states under the Union as a right of force, or a right of sovereignty, and that those who oppose its peaceful exercise, and not those who support it, are culpable; so that the exercise of this right which is a right original, sovereign, and supreme, and not derived from any other human authority, may be, and must be, effected in such a way and manner as the people may for themselves determine. And more especially was this true in the case of the then subsisting government of Rhode Island, which derived no power from the charter or from the people to alter or amend the frame of government, or to change the basis of representation, or even to propose initiatory measures to that end.

In behalf of Borden, the defendant in error, Daniel Webster argued that, "granting that the people are the source of political power, the American principle is that they can exercise this power only through their constituted representatives, and through the votes of properly qualified electors. The right to choose a representative," he declared, "is every man's portion of sovereign power. Suffrage is delegation of political power to some individual. Hence the right must be guarded and protected against force and fraud. That is one principle. Another is, that the qualification which entitles a man to vote must be

prescribed by those laws, directing how it is to be exercised, and also that the results shall be certified to some central power so that the vote may tell. We know no other principle. If you go beyond that, you go wide of the American track * * * . Our American mode of government does not draw any power from tumultuous assemblages."

Thus the question as to which of the two governments was at that time the legal one, and hence the one which could be held correctly to express the will of the state, seemed squarely before the court. But that tribunal did not feel obliged to pass upon the point. It called attention to the provision of the United States Constitution which provides that "the United States shall guaranty to every state in this union a republican form of government, and shall protect each of them against invasion; and on application of the legislature, or of the executive (when the legislature cannot be convened) against domestic violence."[97] Under this article of the Constitution, the Court said, speaking through Chief Justice Taney, "it rests with Congress to decide what government is the established one in the state. For, as the United States guarantees to each state a republican government, Congress must necessarily decide what government is established in the state before it can be determined whether it is republican or not." The court, therefore, held that the question was not a judicial one which it could decide.

It is clear, therefore, that the group will of the state is not to be expressed by every individual or group of individuals, but must follow the duly accepted form provided in the fundamental law of organization.

We may conclude, then, from the above discussion, that the corporate entity has rights of its own; that these rights posit a real group will formulated in a particular manner. It is but a step to inquire: what other elements of group personality are present and attach to the corporate entity? Or, in what ways does this group will manifest itself? Certainly by contract.

[97] United States Constitution, Article 4, section 4.

Certainly by *ultra vires* acts. And certainly in tort. And, at times, by criminal acts. This existence of a will indicates that the corporation is something more than an instrument of legal reasoning, a dialectical device. The fiction theory assumes that it is nothing but this, and, as Professor Freund points out, it ignores the relative psychological unity which gives reality to the conception, and which is necessary to explain the collective attributes of the body corporate.[98] The organic theory, he says, makes this relative psychological unity absolute, and thus carries into the law an unknown hypothetical metaphysical quantity. Under the representation theory, the corporate acts with which the law has generally to deal are not really corporate, but representative. It does not seem to me, however, that these two qualities are mutually exclusive. Granted the necessity of representation in corporate organization, the courts and those who deal with the corporation must, for practical purposes regard all acts of corporate representatives as corporate acts just as the acts of the representative government in a state must be regarded as acts of the state. Rather would it be a more accurate way of speaking to say that the corporate acts with which the law generally has to deal are both really corporate and representative. At least there is a fair presumption that representative acts reflect the corporate will.

Neither the courts nor those who deal with the corporation can be expected to analyze minutely each corporate act to discover whether the representative machinery is functioning according to law and exactly coincides each time with what would be the true corporate will if each member who has the privilege of influencing it actively took advantage of his right. The representative character is always present in corporate acts and the variance of the accuracy with which this exercise of corporate power actually does represent the will of each individual of the group is neither a fair nor an accurate test upon which to determine the moral responsibility of the group for an

[98] Ernst Freund, the Legal Nature of Corporations, p. 83.

act committed under corporate authority. The morality of corporate acts must be traced to the exercise of the corporate will. And this is none the less true because the principle upon which individual rights are exercised must be modified when rights are vested in an association, and the principle of coincidence of discretion and responsibility, of act and liability must yield in some degree to the principle of representation. The courts may rightly hesitate to impute the liability for the act of an agent to a corporation, more so than in the case of an individual principal. But there is no sound reason why it should not be done if it does not appear that some other will than the corporate will should rightly be deemed to have exercised or acquiesced in the liability-creating act.

We cannot, therefore, conclude with Freund that the moral capacity of the aggregate body is generally speaking and for strictly legal purposes an irrelevant factor, nor that it is misleading to assert that every corporate act is the manifestation of corporate will and therefore corporate personality. On the other hand, we believe that it is reasonable to treat every corporate act as a manifestation of corporate will. In Mr. Freund's own words, "if we regard corporate acting capacity as an expression of the principle of representation, and the principle of representation as a product of associated action, irrespective of law, then it follows that the law, by recognizing the corporation as such, does not create its acting capacity, but merely admits the natural effect of the collective holding of rights together with its inevitable incidents." "Thus the recognition of an *ultra vires* act as a corporate act does not involve a logical inconsistency, nor does it prejudge the question of its legality or validity. This, however, leads to a distinction between corporate acting capacity and corporate powers or legal capacity, and while we may admit the former to the fullest extent, we may yet hold that the law in recognizing a corporation grants to it only the powers required for the accomplishment of its charter purposes."

It is submitted, therefore, that where an act is done in the corporate name, but beyond the corporate powers, it is not necessary first to determine whether the act can morally or psychologically be attributed to the body corporate as measured by the degree of actual representation evidenced in the act upon a close examination of each step in the intricate process of formulating the group will. Given the corporate organization with its necessarily representative basis, the conclusion logically follows that the courts must regard every act done by the officers, agents or duly established organs to whom have been committed the power to act in a representative capacity, as in effect the act of the corporation. The familiar doctrine of law by which the intent, as distinct from the motive, will be presumed to exist, in that the law presumes the natural consequences of an act to be intended by the doer irrespective of his motive whether he commits the act in person or by agent, is equally applicable to corporations as to individuals. The very recognition of the group will precludes the necessity of inquiring as to whether or not it is representative in fact as well as in form. The fact of corporate organization conclusively presumes that it is representative.

Corporate Liability in Tort and Crime. That courts are more and more inclined to act upon the presumption that all acts done in the name of the corporation are corporate acts, is evidenced by their attitude towards the liability of corporations in tort and crime. It is true that the tests of the corporate quality of an act are, on the one hand, whether or not the act is done in the corporate interest—that is, for the real or plausible advancement of the common purposes; and, on the other hand, whether it is done by organs whose position is for the doing of this kind of acts representative. That there are exceptions to this latter test, however, has been illustrated by the discussion of State v. Standard Oil Company, above. The fact that the group will sets in motion the act which the

law regards as wrongful, whether the injury be in tort or crime, should not prevent the application of suitable penalties; and if crimes heretofore have been defined in terms of penalties which are not applicable to the corporate entity, the logical step is not to deny liability but to provide suitable penalties. For instance, the New York Court of Appeals has held that a corporation cannot be convicted of homicide under a statute defining that crime as the killing of one human being by the act, procurement, or omission of another.[99]

So far as actual authority goes, courts, as yet, have failed to hold corporations amenable to punishment for homicide. A few states give a remedy by indictment against corporations for negligently inflicting injuries which result in death; but, as those statutes are designed merely to furnish a civil remedy in favor of the estate of the deceased, although in the form of a criminal action, the decisions are of little importance on the question of criminal liability of the corporation for such crimes as homicide. In the case of People v. Rochester Railway and Light Company, the tendency of the late cases is shown to extend the doctrine of corporate civil liability for torts involving personal violence, to criminal prosecutions.[100] Of necessity a corporation could not be indicted for a form of homicide, the only punishment for which is death or imprisonment, as a corporation cannot be subjected to such penalties; but, as to the lesser degrees, at least those not involving actual intent, for which the penalty prescribed is a fine, or both fine and imprisonment, it would seem that, in view of the modern tendency of the courts, a conviction would be possible, provided a statute defining crime was sufficiently broad to permit the inclusion of other than human persons. It is thus evident that it is not the concept of the corporate entity or corporate personality that stands in the way of the courts in convicting corporations of

[99] People of the State of New York v. Rochester Railway and Light Company, 195 N. Y. 102, 88 N. E. 22.

[100] 21 L. R. A., N. S., 998, Note: May a Corporation Be Convicted of Homicide?

crime, but the fact that legislative penalties are not sufficiently broad to include the corporate type of entity within criminal statutes made only in contemplation of the necessity of their application to human persons.

Outside of the question as to whether the statutes of various states are sufficiently broad to comprehend "artificial persons," and the possibility of imposing punishment thereunder, the question is properly one of intent; and in those forms of culpable homicide where intent is essential, the authorities are, as yet, seemingly far from holding that the necessary intent can be imputed to the "artificial person." Thus in Bishop's New Criminal Law[101] it is said to be understood that "the intent essential to murder in the first degree, and the thing itself, would palpably be so far *ultra vires* as to be beyond the competency of the corporation, even if it could be hung in punishment." But it will be noted that the thing which is here standing in the way of recognition of the liability of the corporation is the old and threadbare fiction theory and the failure to distinguish between natural and legal acting capacity.

Again, in McClain's Criminal Law,[102] it is said that "if murder is committed by the officers or agents of a corporation, even though in the prosecution of the corporate business, such acts are the individual acts of the officers and agents, and not the acts of the corporation, it being impossible that such acts could have been authorized, being necessarily *ultra vires.*" And in the American and English Encyclopedia of Law[103] it is said that a corporation cannot be indicted for murder or manslaughter. But none of these statements are convincing in the light of the recognition of a real corporate entity endowed with an undoubtedly real group will, and the increasing discredit accorded the narrow interpretation of the theory of a corporation as merely a "fictitious creature of the law."

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[101] Vol. I, sec. 418.
[102] Sec. 184.
[103] American and English Encyclopedia of Law, p. 845.

It is submitted that if the corporation is held liable in tort for slander, [104] libel,[105] and malicious prosecution,[106] and if it may be held liable criminally for misfeasance and nonfeasance[107] if, moreover, the corporation may be convicted of obtaining property by false pretenses, although that act involves intent to defraud, where by statute the word "person" includes bodies corporate,[108] there is nothing inherent in the nature of the corporation itself to prevent its being held liable for homicide, manslaughter, or similar crimes, merely because intent is a necessary element of the crime. Granted the reality of the corporate will, and neither reason nor experience can deny the exercise of corporate intent, with full resulting responsibility for crime.

Summary of Chapter. The conclusions reached in this discussion of the various theories of corporate existence, we may restate as follows: The theory that a corporation is but an association of individuals and nothing more, is the child of the Roman Law, though it still asserts itself in the minds of the courts and legal writers as an useful insistence upon the necessary connection between the individual and group wills. The second theory—that is, the concept of the Juristic Person—comes from the continental school led by Savigny; it was developed in Germany, and accepted until recently in French law. It is but one branch of the Germanic development which superseded the Roman conception and based its doctrine upon scientific or metaphysical jurisprudence. It insisted upon recognizing realities, but explained them by introducing a fiction to support them. The third theory outlined above is the Realistic Conception of Gierke and his followers. They are the expo-

[104] Citizens Gas and Electric Company v. Black, Ohio State, 115 N. E. 495.
[105] Pennsylvania Iron Works Co. v. Henry Voght Machine Company, 20 Ky. Law Rep. 861, 96 S. W. 551.
[106] Chi. R. I. & P. R. R. Co. v. Holliday, 20 Okla. 680, 120 Pac. 927.
[107] Union Colliery Co. v. Reg. 2 B. R. C. 222, 31 Con. S. C. 81.
[108] State v. Ice and Fuel Co., 166 N. Car. 366, 81 S. E. 737, (1914).

nents of the conservative, as distinct from the ultra-anthropomorphic school. The fourth, or Fiction Theory, is an English adaptation of the Roman Law and Savigny's doctrine, which has taken root in England and America and is now at the beginning of the twentieth century fighting a losing fight with the Realistic Conception. The fifth and sixth theories, which emphasize respectively the objects and the contractual relations of the group, have not assumed any great independent significance in American Law, and can be said to have a rightful place in such a classification as is here presented only as aids to the interpretation of the major theories.

Savigny's Juristic Person theory, Gierke's Real Entity conception, and the English Fictitious Person doctrine are inextricably mingled and confused in the expressions of the courts of the United States as to the nature of the corporation. Doubtless all have had their proper use and have proved to be valuable concepts in aiding the courts to just decisions in particular cases. Courts are not under obligation to be bound to any one political theory or philosophic concept. A concept of political philosophy has no inherent sanctity. If one fits the facts in a given case, judicial action proceeds to adopt it, and rightly so. The administration of justice, and not the definition and establishment of a permanent, immutable, inelastic system of forms, is the fundamental duty and privilege of the Bench. However, it is quite clear to the practicing lawyer, as well as to the observant scholar, that the secondary function of the courts and judges, that of creating or defining a clear and universal system of legal concepts, has assumed the proportions of a primary obligation in the interests of substantial justice.

American law is definitely formulated, however, as to certain aspects of the nature of the corporation. In our system of law, for instance, there can be no doubt that there does exist a separate corporate entity. This is true even though the influence of the English fiction theory still pervades the language of judicial opinions, and to some extent their substance. The corporate entity certainly is recognized as having the power to exercise

rights and to commit wrongs for which the individual members that compose the group incur no individual liability. Thus the corporate entity is said to have a will of its own, an intention, and a capacity for deliberation which may subject it to greater penalties than individuals performing similar acts under like circumstances. Thus, also, it is held to be liable to be subjected to exemplary damages in tort; to a suit for malicious prosecution, for false imprisonment, or for criminal libel. It can appoint an agent and it thereby incurs all the legally inferred rights and obligations that such a status implies. The doctrines of notice and estoppel are forthwith brought into play. Furthermore, the corporate entity can commit fraud through its agent and itself may be the instrument for the attempted perpetration of various types of fraud.

In the field of criminal liability, the courts have not yet generally taken so advanced a position as in the realm of contract and tort. But the trust concept of the relation of directors and officers to stockholders and members is brought into play, and sanctions a close scrutiny of the internal organization of the corporation, and criminal responsibility is placed upon individuals whose liability may be determined. Although the corporate entity has not as such been held liable for the common law felonies, it is quite evident that where a statute has made an act a crime the corporation is subject to such statutory criminal liability if the penalty can be made to apply, and a judgment may be satisfied out of the property of the corporate body. It is but a logical step to recognize full criminal responsibility and provide suitable penalties and statutory definitions broad enough to subject the corporation to punishment wherever its liability may be determined.

Neither the Fiction Theory nor the theory of the Realists is today allowed to stand in the way of a recognition of the closeness of relation between the group will and the will of the individuals that compose the association. Neither the recognition of the corporate entity as a real thing apart from the individuals, nor the treatment of the corporate body as though it

possessed a separate will, need be carried to the extreme of excluding any possible identity of corporate and individual will. If the facts indicate proximity or identity of will, neither the Realist Concept nor the Fiction Theory necessarily excludes relations of agency, nor the application of the doctrines of notice and estoppel. Courts will not hesitate to "look through" or "set aside" the entity,—to "lift the corporate veil"—in order to determine whether particular acts are the acts of the entity, of its members, or of other individuals. And this conception should not be confused by the situation in which the court introduces an additional fiction in the form of its conclusive presumption that all the members of a corporation are, for purposes of suit in the federal courts, to be regarded as citizens of the state of incorporation. Far from disregarding the corporate entity, the cases which present circumstances of agency, notice, or estoppel, or liability of one corporation for obligations of its predecessor, actually assume the existence of the entity, but closely scrutinize its manifold relations in such a way as to give increasing effect to the Realist Theory and proportionate discredit to the Fiction Theory. For the greater the number of acts possible to a corporation, and the broader its rights, the more difficult is it to deny its realty, and, at the same time, the more natural and useful becomes the descriptive term "person."

When the legislatures enact that whenever the word "person" is used in a statute it shall be taken to include corporation unless such an interpretation would be unreasonable, it cannot be said that we are thereby to infer that the legislative body has definitely adopted either the Realist Conception, the Fiction Theory, or the theory of the Juristic Person. It is true that to the layman or the average lawyer these statutes seem strongly to commit the legislatures to the Realist Theory. At least it may be said that they do not imply that this corporate person is a fiction, nor that the entity is to be recognized as an entity merely by the grace of fiction. Yet the language of the courts still clings to the description of the corporate person as a purely fictitious creature of the law existing only in contemplation of

law, a sort of entity imagined or created by a fiction to do justice to the individual members in their group capacity and to those who have dealt with them. At least their inference is that this is a sort of "fictitious person" simply because different from a natural person. Thus is the compromise made between the demands of actual economic conditions in the modern state, and the requirements of exponents of the law who depend upon precedents and maintain that legal forms and concepts should not be unduly disturbed or brushed aside since they are of value as signposts in the law even though long since deprived of reality.

When the courts speak of the fiction of corporate existence they may mean one of several things. The reference may be to the Fiction Theory of the nature of corporate existence as outlined above—that is, that the separate corporate entity is not a reality, but merely treated as such for certain purposes. On the other hand, the reference may be to the idea of the source of corporate life as springing only from an act of the state. This is a secondary phase of the Fiction Theory. The principle was sound in its inception, but is now being rapidly outgrown.

It cannot too constantly be kept in mind that there is an increasing school of Realists in the ranks of the legal writers, and the members of the American Bench and Bar, who have enunciated the reality of the corporate entity. For the most part this enunciation has only a slightly perceptible effect upon the practical relations of the entity. The facts are beyond dispute that the state imposes duties upon people for the protection of the interests of the organized bodies of men called corporations, and the rights correlative to these duties which it allows to be set in motion by the representative wills of individual men designated by the corporate organization. Whether the corporation is real or fictitious, the duties of other people towards it and the laws which enforce the rights correlative to those duties are for the most part the same. The law is administered, and society is carried on in much the same way on either theory.

But there is one practical and far-reaching difference in the rights and duties of the corporation and third persons, which depend upon whether or not the corporation is regarded as real or fictitious. A corporation that is accorded reality, with a corporate will and acting capacity of its own, cannot escape full responsibility for crime any more than a century ago it could, under guise of a fiction, escape compulsory process and full liability, first as principal and then directly, for corporate acts done in contract and tort without corporate seal.

To shift the basis of thinking from the fiction to the realist theory means simply that, instead of the courts regarding the corporate entity as a fiction, a non-reality, and at the same time treating it for all practical purposes as though it were a reality, they will both regard it and treat it as a real entity.

CHAPTER IV.

THE CORPORATE ENTITY AS CITIZEN AND PERSON.

The Citizenship of a Corporation. Ten years before Chief Justice Marshall was called upon to determine the nature of a corporate charter in the Dartmouth College case[109] the Supreme Court of the United States had occasion to determine whether a corporation composed of citizens of one state might sue a citizen of another state in a federal court.[110] The decision of this point turned upon the definition of a corporation. Hence the case becomes of great significance to an inquiry into the nature of the corporation.

The case of Bank of the United States v. Deveaux came before the Supreme Court on writ of error to the circuit court of the United States for the district of Georgia. An action had been brought by the President, Directors and Company of the bank against two citizens of Georgia, Deveaux and Robinson. The bank was a federal corporation chartered by an act of Congress. The record before the court contained an averment that the plaintiffs were citizens of the State of Pennsylvania. The defendants put in a plea to the jurisdiction and argued that the body corporate was not competent to sue in the circuit court of the United States. Upon demurrer by the plaintiff, judgment was rendered for the defendants. In the argument presented for judicial consideration two points were involved. On the one hand, it was urged by the plaintiffs in error that a right to sue in the federal courts was conferred on the bank by the law which incorporated it. It was contended in support of this view, that the incorporating act itself, apart from any pro-

[109] 4 Wheat. 518.
[110] Bank of the United States v. Deveaux, 5 Cranch, 61 (1809).

visions or limitations in the Judiciary Act, [111] conferred jurisdiction upon the circuit court. It was considered that the Judiciary Act in question did not confer such jurisdiction. For the jurisdictional power in the circuit courts, as defined in the United States Constitution,[111x] is dependent upon "the nature of the case as one in law or equity, arising under the constitution or laws of the United States, and treaties made or which shall be made under their authority," or upon the character of the parties.

It was not assumed that the nature of the case could cause jurisdiction to attach. As to cases dependent upon the character of the parties, the Judiciary Act provided that "where the authority of the circuit courts depend on the character of the parties, they derived no jurisdiction from that Act except in the single case of a controversy between citizens of the same state, claiming lands under grant from different states." The facts in the Deveaux case did not present such circumstances. Considering the case from the point of view of its possibly being one arising under a federal law, it was clear, therefore, that unless jurisdiction over the cause had been given to the circuit court by some other federal statute than the Judiciary Act, the bank had no right to sue in that court upon the principle that the case arose under a law of the United States.

The argument was put forward, therefore, that the incorporating act itself conferred the requisite authority. That act, as the court agreed, "creates the corporation, gives it a capacity to make contracts and to acquire property, and enables it to sue and be sued, plead and be impleaded, answer and be answered, defend and be defended, in courts of record, or in any other place whatsoever." But, said the court, "this power, if not incident to a corporation, is conferred by every incorporating act, and is not understood to enlarge the jurisdiction of any particular court, but to give a capacity to the corporation to appear,

[111] 1 Statutes at Large, 73.
[111x] Art. III, sec. 2.

as a corporation, in any court which would, by law, have cognizance of the cause, if individuals." "If jurisdiction is given by this clause to the federal courts," said Chief Jusitce Marshall, "it is equally given to all courts having original jurisdiction, and for all sums however small they may be."[112]

Having struck down the contention that jurisdiction attached because of the "nature" of the case, the court was then called upon to pass upon the plaintiff's argument that jurisdiction was conferred by the character of the parties with reference to diversity of citizenship. This second point is the one upon which the decision turned. Its treatment by the court throws light upon the theories entertained as to the nature of the corporation and enables us to determine whether the corporate entity was regarded as fictitious or real, and whether the court adhered to the logical inferences of the fiction theory as to the separate and distinct existence of the corporate being.

It was argued in behalf of the bank that a corporation composed of citizens of one state may sue a citizen of another state in the federal courts. The jurisdiction of the United States Supreme Court, being limited, so far as respects the character of the parties, to "controversies between citizens of different states," both parties to the cause had to be "citizens" to come within the *descriptio personæ*. Thus the question of whether or not a corporation could be a citizen of a state was fairly presented to the court, and Chief Justice Marshall met it in no uncertain terms. As in the Dartmouth College case, ten years later, he accepted the fiction theory both in language and in fact, but there is no hint that a possible reality might attach to the corporate entity in the particular case, since Marshall decided that, for the purposes of interpreting the United States Constitution, the fiction of separate corporate existence in an exceptional case might be disregarded and the status of the corporate body determined by that of the individuals which composed it.

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[112] Bank of the United States v. Deveaux, 5 Cr. 85, 86.

"That invisible, intangible, and artificial being, that mere legal entity, a corporation aggregate," said the Chief Justice, "is certainly not a citizen, and consequently cannot sue or be sued in the courts of the United States, unless the right of the members, in this respect, can be exercised in their corporate name. If the corporation be considered as a mere faculty, and not as a company of individuals who, in transacting their joint concerns, may use a legal name, they must be excluded from the courts of the Union."[113] The court held that the term "citizen" should be understood as it is used in the constitution, and as it is used in other laws—that is, to describe the real persons who come into court. Those persons in this case, were the real persons, although they came in under their corporate name.

For the purpose of delineating federal jurisdiction, the court refused to accord to the corporate entity a reality distinct from the individual members that composed it. The corporation, it said, was a mere "faculty," and such an "abstraction" was unreal and could not be accorded citizenship. The court felt that, to accord reality to such a corporate entity, was not only contrary to the intent of the fiction theory of corporate existence, but would place it in a difficult position in view of the attitude which it felt called upon to assume as to the scope of the jurisdiction of the federal courts. "The duties of this court," said Marshall, "are to exercise jurisdiction when it is conferred, and not to exercise it where it is not conferred." The inference seems to be that, to grant jurisdiction over the corporate entity in such a case as that presented in the Deveaux case, would be to "usurp the jurisdiction" of other courts. However, it must be kept in mind that the court did grant jurisdiction over this suit, but this was accomplished by looking through the corporate entity to the citizenship of the individual members and allowing jurisdiction to attach by reason of their citizenship. The object in so doing was to allow them the right of the superior degree of protection thought to reside in a fed-

[113] 5 Cranch, 86-87.

eral court as compared with the tribunals of the states. And it must be borne in mind that, had the court decided that a corporation could be a citizen, jurisdiction in this particular case would not have attached if such citizenship had been derived from the place of incorporation because the bank was a federally incorporated body. Hence there would not have been the requisite diversity of state citizenship.

That the court regarded it as a duty to extend federal jurisdiction where the power was given to do so, may be inferred from the following statement: "However true it may be that the tribunals of the states will administer justice as impartially as those of the nation, to parties of every description, it is not less true that the constitution itself either entertains on this subject, or views with such indulgence, the possible fears and apprehensions of suitors, that it has established national tribunals for the decision of controversies between aliens and a citizen, or between citizens of different states. Aliens, or citizens of different states, are not less susceptible to these apprehensions, nor can they be supposed to be less the objects of constitutional provisions, because they are allowed to sue by a corporate name. That name, indeed, cannot be an alien or a citizen; but the persons whom it represents may be the one or the other; the controversy is, in fact and in law, between those persons suing in their corporate character, by their corporate name, for a corporate right, and the individual against whom the suit may be instituted. Substantially and essentially, the members in such a case, where the members of the corporation are aliens, or citizens of a different state from the opposite party, come within the spirit and terms of the jurisdiction conferred by the constitution on the national tribunals."

Thus the court took its stand upon the grounds that the spirit and letter of the United States Constitution warranted it, in this exceptional case, in disregarding the fiction of separate corporate existence. It was in the future to modify and virtually abandon this position by the introduction of an addi-

tional fiction that all the individual members of a corporation are citizens of the state of incorporation.[114]

The decision in the Deveaux case, as the court said, represented the universal understanding on the subject at that time. But that part of the fiction theory which accords separate existence to the corporate entity was disregarded. That is, corporate existence being considered but a fiction itself, the court evidently believed that the situation in that particular case was one in which there had been an attempt to press a legal fiction to an extent beyond its original purpose.

In support of his argument, that the citizenship of the individuals composing the corporation was the real citizenship to be considered in the case, Chief Justice Marshall said: "The common understanding of intelligent men is in favor of the right of incorporated aliens, or citizens of a different state from the defendant, to sue in the national courts. It is by a course of acute, metaphysical, and abstruse reasoning, which has been most ably employed on this occasion, that this opinion is shaken." And the court took occasion to say that, "our ideas of a corporation, its privileges, and its disabilities, are derived entirely from the English books; we resort to them for aid, in ascertaining its character. It is defined as a mere creature of the law, invisible, intangible, and incorporeal. Yet, when we examine the concept further, we find that corporations have been included within terms of description appropriate to real persons."

The court, however, did not accord reality to the corporate entity. It chose to regard the controversy as of the class of suits "substantially between aliens, suing by a corporate name, and a citizen, or between citizens of one state, suing by a corporate name, and those of another state." But, said the court, "when these are said to be parties to the controversy the court does not mean to liken it to the case of a trustee. A trustee is a real person capable of being a citizen or an alien, who has

[114] Louisville, C. & C. R. R. v. Leston, 2 How. 497.

the whole estate in himself. At law, he is the real proprietor, and he represents himself, and sues in his own right. But in this case the corporate name represents persons who are members of the corporation." And it was broadly held that if the constitution would authorize Congress to give the courts of the Union jurisdiction in this case in consequence of the character of the members of the corporation, then the Judiciary Act should be construed to give it.

The decision in the Deveaux case is not an absolute avowal that the corporation is not in any case to be regarded as an entity distinct from its members. The court goes only so far as to say that in determining the matter of the jurisdiction of federal courts dependent upon the citizenship of the parties under the United States Constitution, the corporate entity will not be regarded as having a distinct citizenship apart from that of the individuals who compose it. This is not even a statement that under no circumstances will a corporation be regarded as having citizenship. For the court recognized the fact that corporations composed of individual citizens had been considered by legislatures as citizens, under certain circumstances. This, for instance, said the court, was to be strongly inferred from the Registering Act. "It could never be intended that an American registered vessel, abandoned to an insurance company composed of citizens, should lose her character as an American vessel; and yet this would be the consequence of declaring that the members of the corporation were, to every intent and purpose, out of view, and merged in the corporation." Yet even these cases did not regard a citizenship of the corporation apart from that of the individuals.

The court did not give reasons that might be inferred from the nature of the corporation, by which it differentiated between cases of recognized English authority which had held corpora-

tions to be "occupiers" and "inhabitants"[115] within certain statutes, and those which denied citizenship in jurisdictional disputes, other than that the opinions in the former class of cases were not precisely in point as precedents. The cases were cited rather as serving to show "that, for the general purposes and objects of a law, this invisible, incorporeal creature of the law may be considered as having corporeal qualities." Indeed, the court indicates that it might have been quite as willing to consider the corporation as a "citizen" as it would an "inhabitant" or "occupier," for the particular purpose of such statutes. By so doing, however, it argued, there would be no precedent established binding upon the court to consider the corporation as a citizen. Citizenship for the purposes of acquiring jurisdiction in the federal courts would be an exception to such a rule if established. Thus the court said: "It is true that as far as these cases go they serve to show that the corporation itself, in its incorporeal character, may be considered as an inhabitant or an occupier, and the argument from them would be more strong in favor of considering the corporation itself as

[115] A statute of Henry VIII concerning bridges, and highways, enacts that bridges and highways shall be made and repaired by the "inhabitants of the city, shire, or riding," and that the justices shall have power to tax every "inhabitant of such city," etc., and that the collectors may "distrain every inhabitant as shall be taxed and refuses payment thereof, in his lands, goods, and chattels." Under this statute those had been considered inhabitants who held land within the city where the bridge to be repaired lay, although they resided elsewhere. Lord Coke said: "Every corporation and body politic residing in any county, riding, city or town corporate, or having lands or tenements in any shire, *quae propriis manibus et sumptibus possident et habent*, are said to be inhabitants there, within the purview of this statute." The tax was not imposed on the person, whether he were a member of the corporation or not, who resided on the lands, and it was imposed on the corporation itself, and consequently, as the court said in the Deveaux case, "this ideal existence is considered as an inhabitant, when the general spirit and purpose of the law requires it."

In the case of the King v. Gardner in Cowper, 79, a corporation was decided by the court of Kings Bench, to come within the description of "occupiers or inhabitants." In that case Lord Mansfield notices and overrules "an inconsiderate dictum" of Justice Yates, that a corporation could not be an inhabitant or an occupier.

endowed for this object and purpose with the character of a citizen, than to consider the character of the individuals that compose it as a subject which the court can inspect, when they use the name of the corporation, for the purpose of asserting their corporate rights. Still the cases show that this technical definition of a corporation does not uniformly circumscribe its capacities, but that courts for legitimate purposes will contemplate it more substantially." This last sentence indicates that the doctrine of the Deveaux case is based on what the court regards as an exception to the usual treatment of the corporation.

In conclusion of the discussion of the Deveaux case, it may be said that it seems to be the first case before the United States Supreme Court in which an answer may be found to the question: When will the courts disregard the corporate entity and deal with the natural persons that compose the corporation? There is not here, as in many of the later classes of cases which the answer to this question includes, any allegation or suggestion of fraud upon the court, like that in the cases where a corporation is formed under the laws of a foreign state for the sole purpose of obtaining jurisdiction of the federal tribunal over a suit between the individual incorporators and other persons citizens of the same state. That class of cases, it will be seen, could only have arisen after the Supreme Court in effect abandoned the doctrine laid down in the Deveaux case by introducing the conclusive presumption that the citizenship of the individual members is the same as that of the state of incorporation.

It is important, therefore, to note the reasons why the court arrived at its decision to modify its original doctrine. Before proceeding with that discussion, however, it may be said, finally, that the decision in this case was based primarily on precedent, and only secondarily on any reasoning as to the nature of the corporation. The English case which the court thought precisely in point on the question of jurisdiction was Mayor and

Commonwealth of London v. Wood.[116] In that case the corporation of London brought suit in its corporate name against Wood, in the mayor's court. The suit was brought by the mayor and commonalty, and was first tried before the mayor and aldermen. The judgment rendered in the case was brought before the court of the King's Bench and reversed, "because the court was deprived of its jurisdiction by the character of the individuals who were members of the corporation." In that case, said Chief Justice Marshall, "the objection that a corporation was an invisible, intangible thing, a mere incorporeal legal entity, in which the characters of the individuals who composed it were completely merged, was urged and considered. The judges unanimously declared that they could look beyond the corporate name, and notice the character of the individual."

What the court said in the Deveaux case is broadly enough stated so that it may be regarded as the opinion of the United States Supreme Court at that time, both with reference to corporations of the various states as well as to those incorporated under federal law. The two other cases[116x] in the group usually cited with this case did not involve federal corporations, but dealt with state-chartered bodies. The court's decision to look to the citizenship of the members of the corporation and allow them to sue in their corporate names, necessarily applied to a state organization as well as a federal one,[117] and this was accepted as a settled rule of the courts.[118]

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[116] 12 Mod. 669.

[116x] Hope Insurance Company v. Boardman, 5 Cr. 57; Maryland Insurance Company v. Wood. See arguments in the Deveaux case, 77. For a discussion of the bearing of these cases upon the position of the foreign corporation in American Constitutional Law, see Henderson's book on that subject, pp. 39, 54-57.

[117] The previous case of Turner v. President and Directors and Company of the Bank of North America, 4 Dall. 8 (1799), was a suit by a Pennsylvania corporation in North Carolina. Chief Justice Ellsworth said: "The action below was brought by the president and directors of the Bank of North America who are well described to be citizens of Pennsylvania." But the matter was not argued and the court in the Deveaux case did not consider the case an authority.

[118] Angell and Ames (1st ed.), 212 ff. Henderson, Position of the Foreign Corporation in American Const. Law, p. 39.

This was the law until about 1840. Up to that time, as Dr. Willoughby points out in his Constitutional Law,[119] the "doctrine prevailed that a corporation being an artificial unit, the court would look behind its corporate personality to see whether the individuals of which it was composed were, each and every one of them, citizens of a state different from that of each of the parties sued."[120] But in later cases this doctrine was repudiated, and the principle stated, first, that the citizenship of the individuals composing the corporation is to be presumed to be that of the state by which the corporation was chartered, and, still later, that this presumption is one that may not be rebutted." Thus, in Ohio and Mississippi Railroad Company v. Wheeler[121] the court said, citing Louisville, C. and C. Railroad Company v. Leston:[122] "Where a corporation is created by the laws of a state, the legal presumption is that its members are citizens of the state in which alone the corporate body has a legal existence; and that a suit by or against a corporation, in its corporate name, must be presumed to be a suit by or against citizens of the state which created the corporate body; and that no averment or evidence to the contrary is admissible, for the purpose of withdrawing the suit from the jurisdiction of a court of the United States."

Today there is said to be a presumption as to corporations that they are citizens and residents of the state creating them.[123] The discussion of cases in Volume 11 of the Lawyers' Reports Annotated[124] clearly presents the view that it is now the settled rule that corporations, for all purposes of federal jurisdiction,

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[119] Willoughby, Constitutional Law, Vol. II, sec. 568.
[120] Bank of Vicksburg v. Slocomb, 14 Pet. 60.
[121] 1 Black, 286; 17 L. ed. 130.
[122] 2 How. 497; 11 Law Ed. 353.
[123] Speer, Rem. Causes, 33, note, citing National S. S. Co. v. Tugman, 106 U. S. 118, 27 L. ed. 87; Ohio and M. R. Co. v. Wheeler, 66 U. S. (1 Bl.) 286, 17 L. ed. 130; Ex parte Schollenberger, 96 U. S. 369, 24 L. ed. 853; B. & O. Co. v. Harris, 79 U. S. (12 Wall.) 65, 20 L. ed. 354; Chi. & N. W. Rd. Co. v. Whitton, 80 U. S. (13 Wall.) 270, 20 L. ed. 571.
[124] 11 L. R. A. 216, Note.

are conclusively considered as citizens of the state which creates them, and no averment or proof as to citizenship of its members elsewhere is competent or material. Where, however, the corporation is chartered in several states, when sued in one state, it cannot remove the case to the federal court on the ground of its citizenship in the other state.[125] The mere declaration by the state that the corporation shall be deemed a citizen is not enough. The Supreme Court has so held where the corporation was originally incorporated in one State, and then reincorporated in another, the first state alone determines citizenship.[126]

Thus a new fiction has been added to the already complex group of fictions as to the nature of corporate existence. That this irrebuttable presumption is truly a fiction is evident when it is considered that one of the individual stockholders may sue a corporation, and the court will recognize in him a citizenship different from that accorded him as a member of the corporation. In such a case a stockholder may assert that he is a citizen of one state and at the same time describe himself as a stockholder of a corporate body all of whose members the federal courts will conclusively presume to be citizens of another state.[127]

Such a case was that of Doctor v. Harrington.[128] A New Jersey citizen, stockholder in a New York corporation, brought a stockholder's bill in the federal court in New York. Since jurisdiction depended on the doctrine of indisputable citizenship, he necessarily alleged that there was a conclusive presumption that all the stockholders were citizens of New York. The defendant replied, with unanswerable logic, that by so alleging he alleged himself out of court, since there necessarily arose an irrebuttable presumption that the plaintiff himself was a citizen of New York. The Supreme Court, however, following sense rather than logic, sustained the jurisdiction, "frankly

[125] Memphis and C. R. Co. v. Alabama, 107 U. S. 581, 27 L. ed. 518.
[126] St. Louis and San Francisco Ry. v. James, 161 U. S. 545 (1896). And see Henderson, Op. Cit., pp. 194, 73.
[127] Willoughby, United States Constitutional Law, Vol. II, sec. 568, p. 985.
[128] 196 U. S. 579 (1905).

admitting," as Henderson says, "that the presumption of citizenship was a pure fiction, devised for no other purpose than to enable the court to assume a jurisdiction which it believed the constitution did not confer."[129]

The Corporate Entity as Alien Enemy. The Deveaux case and the doctrine announced therein, that the court would, under exceptional circumstances, look beyond the corporate entity to the natural persons composing it, was expressly founded upon an English precedent. It is of very great interest, therefore, to find, over a century later, the highest court in England turning to Marshall's opinion as itself a precedent to justify the House of Lords in looking beyond the corporate entity to be guided by the status of the corporators. True, the expression of the House of Lords on this point is embodied in a dictum, and the question before the court concerned not a matter of citizenship, but of the residence of a corporation for purposes of ascertaining its character as friend or enemy under the Trading With the Enemy Acts. In Daimler Company, Ltd., v. Continental Tyre Company (G. B.), Ltd.,[130] the actual point upon which the judgment rested was whether the secretary of the Continental Tyre Company had authority, in the absence of an express stipulation, to bring a suit in the interests of his company during war time, for the payment of three ninety-day bills of exchange, against the Daimler Company. The latter company was a British Company registered in England. The secretary of the Continental Company was a naturalized British subject of German nationality, resident in England at the time the war broke out. The Continental Company was owned, as to the majority of its stock, by a German corporation in Germany, and by three other German stockholders and directors. Its secretary was the only stockholder and representative in England after the outbreak of the war between England and

[129] Henderson, Position of Foreign Corporations in American Constitutional Law, p. 76.

[130] 114 Law Times Report, 1049 (H. of L., 1916).

Germany. He relied, for authority to bring the suit, upon an express stipulation in the minutes of the corporation, which, however, when the minute book was produced, failed to appear. On the point of the agent's authority, therefore, it was held that the common law and British statutes[131] on the subject of trading with the enemy in time of war make all the other directors and stockholders, who were residents in Germany, enemy aliens. And hence, since the evidence upon which the secretary relied did not show that the directors had at any time before the war granted an express power to act as the agent of the corporation for the general purposes of bringing suits in its behalf, and since the secretary did not and could not claim that they could do so after the outbreak of the war without violating the law against trading with the enemy, he was powerless to bring the suit. This was the point upon which the House of Lords reversed the decision of the Court of Appeals.

It was not necessary for the court to go further and consider the nature of the corporation, and whether or not it could itself become an enemy alien though an English registered company. They did, however, believe it of sufficient importance to discuss at length. The Deveaux case was cited by Lord Parker.

As I have said, the question raised was not as to the citizenship of the Continental Tyre Company for the purposes of determining whether or not the court had jurisdiction of the suit. The issue was whether or not the rule as to the "residence" of a company, set forth in the British Companies Act,[132] which held that a company registered in England should be regarded for purposes of suit as having its residence in England, should not be modified in view of war conditions and the peculiar problems arising from questions of "trading with the enemy." It was granted that under the Companies Act, for

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[131] Trading With The Enemy Act, Sept. 18, 1914, 4 & 5 Geo. V, c. 87, s. 1, sub-sec. (2); and see the former Act passed in August, 1914, and the later Trading with the Enemy Act of Nov. 27, 1914, which provided for the appointment of an Alien Property Custodian.

[132] British Companies Act, 1908.

of alien enemies was put under surveillance to such an extent that payments made or transactions carried on with such a company in this country would have been under official inspection." It appeared to Lord Shaw, therefore, to be a "somewhat strong proposition under these circumstances to hold that one is entitled to go behind the English incorporation of the company and to declare that all of the statutory stipulations were vain, seeing that such a company was an enemy, to trade with whom, directly or indirectly, was a misdemeanor."

Lord Atkinson believed that the actual "residence" of a company for the purpose of determining its enemy character, as in the case of the administration of the income tax laws, should be held to be the real business center from which the governing and directing mind of the company or its directors operate. He pointed out that the lower courts had not had the minute book of the Continental Company before them in weighing the evidence and making their decision as to the residence of the company for determining its enemy character, and he concluded that "the embarrassing, and, rather unfortunate result of this admission is, that the full facts, showing in what country—England or Germany—lay the real business centre from which the governing and directing mind of the company or its directors operated, regulating and controlling its important officers, were, save so far as revealed in the evidence of its secretary, never disclosed. These are, however, the very things which, for the purpose of income tax at all events, have been held to determine the place of residence of a company, like the respondent company, so far as such a fictitious legal entity can have a residence."[135] And "I see no reason why, for the purpose of deciding whether the carrying on by such a company of its trade or business does or does not amount to a trading with the enemy, they should not equally determine its place of residence. It is well established that trading with the most loyal British sub-

[135] Citing De Beers Consolidated Mines, Ltd., v. Howe, 95 L. T. Rep. 221; (1906) A. C. 455.

"From and after the date of this proclamation the following prohibitions shall have effect (save so far as licenses may be issued as hereinafter provided): we do hereby accordingly warn all persons resident carrying on business or being in our dominions: (1) not to pay any sum of money to or for the benefit of an enemy." In section three of that proclamation the term "enemy" is defined as follows: "The expression enemy in this proclamation means any person or body of persons of whatever nationality resident or carrying on business in the enemy country, but it does not include persons of enemy nationality who are neither resident nor carrying on business in the enemy country. In the case of incorporated bodies, enemy character attaches only to those incorporated in an enemy country."

It appeared to Lord Shaw that "this was a plain guide and instruction to persons in the position of the appellants. They were told first that a transaction permitted under proclamation should not be deemed trading with the enemy, and secondly, that in the case of incorporated bodies enemy character attached to those incorporated in an enemy country; but, thirdly, that it attached only to those. I think, in short, that it was a very plain intimation that if a company was not incorporated in an enemy country, but was incorporated in our own country, then this was, though negatively expressed, the exact case in which a payment to such a company became unexceptionable and legitimate." And he pointed out that it was not to be forgotten that under the very same statute provisions were enacted to cover the case of companies whose share capital or directorate was either wholly or in certain proportion held by alien enemies.[184] It was clear, even under the Act of September 18th alone, that "the case of companies held by a majority or even by a minority

[184] Trading with the Enemy Act, 1914, 4 & 5 Geo. 5, c. 87, sec. 2 (2), provided that in the case of such a company, when a third or more of the issued share capital or the directorate was so held the Board of Trade might obtain authority to inspect the books, * * * and to appoint an inspector. By section 3 further precautionary provisions were made giving to the Board of Trade power to apply to the court for the appointment of a comptroller.

vant if the question for decision was whether the company had not held out the secretary to third parties as possessed of these powers in such a way as to estop them, as against those parties, from repudiating the secretary's authority, but that is not the question for decision. It is no doubt true that when a secretary of a company is found doing certain things in the name of, and on behalf of his company, which could regularly be authorized by it, and no resolution or minute is provided authorizing him to do the things, the maxim *'omnia præsumuntur rite esse acta'* will be applied and the necessary authority will be presumed to have been lawfully given him." But this maxim could not, thought his Lordship, "legitimately be applied where the agent vouches a particular document as the source of the authority he claims to exercise, and it is found that the document when produced gives him no such authority. It cannot be presumed he got the authority by means he has on oath repudiated. His oath rebuts the presumption."[137]

The majority of the Lords did not adopt Lord Atkinson's view that the proper criterion for determining the residence of the Continental Company was the real business center from which the governing and directing minds of the company or its directors operated. Moreover, the majority opinion denied the application of the provisions of the Companies (Consolidation) Act of 1908, that a company registered in England should be considered as a resident of that country, for all purposes. But, as Lord Parker's judgment indicates, they did not accept Lord Shaw's view of the application of the Trading With the Enemy Acts and Proclamation of September 9th, which acts provided that "the enemy character attaches only to those (companies) incorporated in an enemy country."

Lord Parker's judgment accepted the residence of the Company as in England, but adopted an argument similar to that of Lord Atkinson in the latter's discussion of legal residence as dependent upon the place of control. Lord Parker reached the

[137] 114 L. T. Rep. 1049, 1053.

conclusion that, although a resident of England, the Company as a matter of fact was of enemy character. In so holding, he not only, in effect, expressed himself as taking exception to the express stipulation in the proclamation under the Trading With the Enemy Act, but clearly and strongly went on record as recognizing an exception to the doctrine in the Anglo-American fiction theory of corporate existence which holds that the corporate entity is an absolutely separate and distinct entity apart from the individuals that compose it.

"By this decision," says the Law Times,[138] "the separate-entity theory of the statutory company has received a very rude shaking." This, however, does not represent the case accurately. That theory received no more of a shock than it might be said to have received in the decision more than a generation before in State v. Standard Oil Company.[139] The only sort of a shaking it did receive was such as is always resorted to in the light of common sense when the theory of separate corporate entity is sought to be translated into terms of an absolute divorce of the will of the entity from that of its incorporators. "No one can question," said Lord Parker, "that a corporation is a legal person distinct from its corporators, and that the relation of a shareholder of a company, which is limited by shares, is not in itself the relation of principal and agent or the reverse; that the assets of the company belong to it and the acts of its servants and agents are its acts, while its shareholders, as such, have no property in the assets and no personal responsibility for those acts. The law on the subject is clearly lain down in the passage in Lord Halsbury's judgment in Salomon v. Salomon and Co.[140] 'I am,' he says, 'dealing with the provisions of the statute, and it seems to me to be essential to the artificial creation that the law should recognize only that artificial existence apart from the motives or conduct of individual corporators * * * .

[138] Vol. 142, p. 18, Nov. 11, 1916. This opinion has been followed in America by the Law Reviews.

[139] 49 Ohio St. 137; *supra*, pp. 43ff.

[140] 75 L. T. Rep. 426; (1897) A. C. p. 30.

Short of such proof'—that is, proof in appropriate proceedings that the company had no real legal existence—'it seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person, with its rights and liabilities appropriate to itself, and that the motives of those who took part in the formation of the company are absolutely irrelevant in discerning what those rights and liabilities are.'" "I do not think," Lord Parker went on to say, "that it is a necessary corollary of this reasoning to say that the character of its corporators must be irrelevant to the character of the company; and this is crucial, for the rule against trading with the enemy depends upon enemy character."[141]

This necessarily close relation between the wills of the individual incorporators and the will and action of the corporate entity is a thought which it is hoped this study may impress upon the mind of the reader. It does not imply a denial of the separate entity nor a condition of absolute divorce of group will and individual will. It is not necessary to conclude, with Lord Parker, that the status of the individual members of the corporation is to be attributed to the corporation, whether it be a status of alien enemy character as in the Continental Tyre Company case, or one of state citizenship as in the Deveaux case. However, the special status referred to as "enemy character" under the war-time laws of trading with the enemy is a sufficiently important and exceptional case to warrant the court in looking to the status of the individual shareholders to assist in determining the alien enemy status *vel non* of the corporation. For it is of capital importance to discover whether a British subject who owes loyalty and allegiance to the British Crown can legally perform certain acts without subjecting himself to prosecution for trading with the enemy.

The act of a corporate entity may properly be traced to the control over it exercised by its shareholders, agents, or directors.

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[141] 114 L. T. Rep. 1059.

In this control, I believe Lord Parker has touched upon the keynote of a commendable modern tendency of the court in dealing with corporations, which must be increasingly recognized as sound in its application to the administration of justice. In the control exercised by the shareholders or directors, or both, over the agencies of corporate activity, his Lordship finds an analogy between the "artificial" person and the natural person, by which the former is said, in effect, to maintain a "commercial domicile" in an enemy country through the fact of control exerted from that source, which places it in the class of alien enemies. Enemy character, Lord Parker states, depends upon residence or commercial domicile. "A natural person, though an English-born subject of his Majesty, may bear an enemy character and be under liability and disability as such by adhering to his Majesty's enemies. If he gives them active aid, he is a traitor; but he may fall short of that and still be invested with enemy character. If he has what is known in Prize Law as a commercial domicile among the King's enemies, his merchandise is good prize at sea, just as if it belonged to a subject of the enemy power. Not only actively, but passively, he may bring himself under the same disability. Voluntary residence among the enemy, however passive or pacific it may be, identifies an English subject with his Majesty's foes. I do not think it necessary to cite authority for that well-known proposition."

Now, says Lord Parker, how are such rules to be applied to an artificial person, incorporated by forms of law? "As far as active adherence to the enemy itself, there can be no difference except such as arises from the fact that a company's acts are those of its servants and agents acting within the scope of their authority."[142] In the case of an artificial person, is there an analogue to voluntary residence among the King's enemies? "Its impersonality," he says, "can hardly put it in a better position than a natural person and lead to its being unaffected by any-

[142] An illustration of the application of such rules to a company (as it happens, a company of neutral incorporation, which is an *a fortiori* case) is to be found in Netherlands v. Fisher, 18 Times Law Rep. 116.

thing equivalent to residence. It is only by a figment of speech (and herein he endorses the idea that corporate existence is still to be spoken of as founded in fiction) that a company can be said to have a nationality or residence at all. If the place of its incorporation under municipal law fixes its residence, then its residence cannot be changed, which is almost a contradiction in terms, and in the case of a company residence must correspond to the birthplace and country of natural allegiance in the case of a living person, and not to residence or commercial domicile."

It should be pointed out that this statement of Lord Parker—that is, "if the place of its incorporation under municipal law fixes its residence, then its residence cannot be changed, which is almost a contradiction in terms,"—suggests an idea which does not seem to be sufficiently emphasized in the judgments of the other Lords in this case: namely, that there may be more than one sort of residence attaching to a person or entity. The residence of the corporation designated as at the place of registry does not, it seems to me, exclude the possibility of a *de facto* residence similar in kind to the foreign commercial domicile which a natural person may maintain. A frank recognition of such a fact would not have involved the court in the necessity of disregarding the express terms of the proclamation of September 9th and the Trading With the Enemy Act of September 18th, 1914. Nor would it have required Lord Parker to set up the relation of control between shareholders, directors and agents of a corporation as a sort of new fiction, and "analogue" to the voluntary residence among the King's enemies maintained by a natural person. For, this is no more than pure fiction under the facts in the Daimler case. "Voluntary" residence among the King's enemies means the will to reside there, either actively or passively expressed. There certainly was no corporate will of such a nature evidenced in this case. And there is much weight in Lord Shaw's opinion that "by the Act to amend the Trading With the Enemy Act of 1914, passed on the 27th November last, various provisions were made for the constitution of an office of custodian of enemy property; the

custodian being appointed to hold such property 'until the termination of the present war,' and thereafter to 'deal with the same in such manner as his Majesty may by Order in Council direct. So far as Parliament is concerned, the situation is, as stated, that the country of incorporation of the company, if England, excludes the company from being either an enemy company or of an enemy character, and all the provisions relative to the working of a company whose shareholders are mixed are provisions which proceed upon that foundation.' "

Lord Shaw was "accordingly of opinion that the official of the Daimler Company, charged with the payment of monies, had he ventured to make payment of the debt due by that company to the Continental Company or to a person properly acting as its representative, would have been safe in doing so and guilty of no misdemeanour."[143]

This opinion seems to me to be the most logical way to proceed in the matter. It is in harmony with the method of management of the property of alien enemies, both corporations and individuals, by the Alien Property Custodian in the United States during 1918-1919 when this country was a belligerent. And had a like situation arisen in the United States, certainly, by reason of our constitutional theory which provides that the acts of the legislature, if constitutional, are binding upon the courts, the United States Supreme Court would not have been at liberty to make a decision contrary to the express act of the national legislature.

It is to be regretted that an excrescence in our own law,—an exception to the fiction theory of corporate existence which could not stand without a second fiction to bolster it up, and which faces inevitable death in the near future,—should have been seized upon by Lord Parker to justify his theory that enemy status of the majority of the corporators could be attributed to the corporation itself. Lord Parker referred to the

[143] This was one of the two main points in the case. The majority of the Lords supported this conclusion, but not the reasoning.

Deveaux case as a precedent. His discussion of that case is both enlightening to an understanding of the status of that phase of the fiction theory in the United States, and to the weight with which it is evidently regarded in England. "So far as I can find," he says, "this precise question (that is, as to whether resort is not to be had to the predominant character of the shareholders and corporators) has been asked heretofore once, and once only; namely, in argument in the case of Bank of the United States v. Deveaux,[144] and the judgment of Marshall, C. J., did not answer it, though he decided the case in favor of the party whose counsel suggested this point as part of a wider argument. Accordingly, all that can be said is that the suggestion cannot have shocked that great jurist, and his actual decision proceeds upon the assumption that for certain purposes a court must look behind the artificial *persona*—the corporation—and take account of and be guided by the personalities of the natural persons, the corporators."

"In the Court of Appeal the Lord Chief Justice expressed the opinion that the judgment of Marshall, C. J., had not been approved in later cases before the Supreme Court of the United States. I have examined the cases in question—the Louisville, Cincinnati, and Charleston Railroad v. Leston, [145] and St. Louis and San Francisco Railway Company v. James[146]—and have come to the conclusion that, so far as is material to the question in hand, they do not bear out this criticism. This is how the matter stands: Under the Constitution of the United States jurisdiction is given to Federal Circuit Courts to decide controversies between 'citizens' of different states. In the case in question Marshall, C. J., held that an artificial person could not be a citizen for this purpose, but, not to deny justice to a corporation, he took cognizance of the corporators, and finding them all to be citizens of the state which had incorporated the plaintiff bank, he admitted jurisdiction and treated the bank

[144] 5 Cranch, at p. 81.
[145] 2 How. 497.
[146] 161 U. S. 545.

like a citizen of that state and entertained the suit. It was afterwards contended, and for some time with success, that this decision applied only when all of the corporators were citizens of that state and that it required a refusal of jurisdiction, when some of them were citizens of another state. It was in this stage that he expressed the doubts referred to in the judgment below. Long after this time the matter was at last set at rest in the case of the St. Louis Railway, when the court surveyed all the different phases of the controversy. Remarkable is the way in which this was done. The federal courts did not ignore the existence of the corporators, fixed their attention on the place where the corporation was chartered, or the state under whose laws it was registered. They continued to fix their attention on the citizen incorporators, but they conclusively and incontestibly presumed that they were all citizens of the state of the incorporation. Such bearing, therefore, as these cases have on the present question is in favor of the appellants (that is, the Daimler Company's defence that the Continental Company was of enemy character), for it is plain that great judges, trained in the principles of the English Common Law, have not found it contrary to principle to look at least for some purposes, behind the corporation, and consider the quality of its members."[147]

The Daimler case has already been discussed at some length. It seems of sufficient importance, however, to merit a discussion from two other points of view. In the first place, as I have pointed out, Lord Parker employed a sort of new fiction: the idea of control as an analogue to the commercial domicile of a natural person. This idea is a vital one, and it will not be strange to see the courts apply it more widely in the future, as they have in the United States in the past generation,[148] to prevent the use of the corporate form as a cloak to commit fraud.

[147] Lord Parker makes a somewhat similar observation upon the case of Janson v. Driefontein Consolidated Mines, 87 L. T. Rep. 372; (1902) A. C. 484.

[148] See discussion of cases at pp. 142ff below.

Lord Parker speaks of "control, an idea which if not very familiar in law, is of capital importance, as very well understood in commerce and finance. The acts of a company's organs, its directors, managers, secretary, and so forth, functioning within the scope of their authority, are the company's acts and may invest it definitely with enemy character." It seems to him "that similarly the character of those who can make and unmake those officers, dictate their conduct mediately or immediately, prescribe their duties and call them to account, may also be material in a question of the enemy character of the company." In this, as I have pointed out, it seems to me that there is an unnecessary identification of "status" and "action." "If not definite and conclusive," says his Lordship, "it must at least be *prima facie* relevant as raising a presumption that those who are purporting to act in the name of the company are, in fact, under the control of those whom it is their interest to satisfy. Certainly, I have found no authority to the contrary."

And he contends that "such a view reconciles the position of natural and artificial persons in this regard, and the opposite view leads to the paradoxical result that the King's enemies, who chance during war to constitute the entire body of corporators in a company registered in England, thereby pass out of the range of legal vision, and, instead, the corporation, which is in itself incapable of loyalty, or enmity, or residence, or of anything but of bare existence in contemplation of law and of registration under some system of law, takes their place for almost the most important of all purposes, that of being classed among the King's friends or among his foes in time of war."[149]

This last sentence suggests the second and last viewpoint from which I wish to call attention to the judgments in this case: namely, the attitude of the Lords towards the corporate entity and the bearing which their expressions have upon the fiction theories of corporate existence. I mention the views of Lord Parker's opinion more in detail than those set forth in the other

[149] 114 L. T. Rep. 1059.

five opinions in the case, not only because his is the clearest and most convincing in its reasoning, but also because it seems to have had as great weight as any of the judgments in the decision of the case. Viscount Mersey stated that he had written a judgment, but thought it better to withdraw it in favor of Lord Parker's, in which, he said, his reasons were fully expressed. Lord Atkinson, having come to the conclusion that, because of the want of any express authority in the secretary of the Continental Company to bring the suit, an appeal should have been granted, said: "I do not desire to express any opinion on the other and main point raised in the case, further than to say that the question of residence of the company apart, I do not think that the legal entity, the company, can be so identified with its shareholders, or the majority of them, as to make their nationality its nationality or their status its status, so completely as to make it an alien enemy because they are alien enemies, or to give it an enemy character because they have that character. I think the judgment of Lord MacNaughten in Jensen v. Driefontein Consolidated Mines, Ltd.,[150] is inconsistent with any such view. I think it is much to be regretted that the appellant company were not permitted to defend, as in my opinion they should have been, so that all of the facts might have been elicited, and it could be determined whether the company resides and trades in Germany or not. I think the order suggested by my noble and learned friend Lord Parker should be made."

From this discussion and that which preceded it, it is evident that Lords Atkinson and Shaw were not in accord with Lord Parker in his argument that the status of the shareholders might be attributed to the corporate entity. Lord Shaw made the pertinent inquiry whether a majority would determine the

[150] 87 L. T. Rep. 372, (1902) A. C. 484. Speaking of the Transvaal Company, Lord MacNaughten said: "If all its members had been subjects of the British Crown the corporation itself would have been none the less a foreign corporation and none the less in regard to this country alien."

matter, with the possible result of seriously injuring large minorities of British shareholders; and, indeed, whether a company whose shares might be transferred from day to day stood to change into and out of its character as an alien enemy in consequence of the change of personnel of its shareholders.[151]

Neither Lord Atkinson nor Lord Parker denied the separate entity of the corporation. Lord Atkinson said that "if a company should not have and not be able lawfully to appoint any directors other than alien enemies, then, though the legal entity, the company, might continue to exist, its action in its trade in this country would be paralyzed on point of law, the status of its agents as distinct from its shareholders rendering it incapable of making any contract."[152] "I do not think," he said, "that the legal entity of the company can be identified with its shareholders."[153]

Lord Shaw, however, did not believe the entity should be treated as a "person" like a natural person. He declared that "allegiance and loyalty are personal, by the nature of the case," and that "the application of such ideas to a limited company is incongruous,"[154] for "an incorporated company cannot with propriety have such terms applied to it, as if it were a mind subject to emotions or passions or a sense of duty." He was inclined to emphasize the idea of a corporation as primarily a business device. "It is," he said, "a creation of the law convenient for the purposes of management, of holding of property, of the association of individuals in business transactions, in short for all purposes and with the limitations set forth in the Companies Act."[155]

In accord with this view, is that of the Earl of Halsbury. He agreed that the order suggested by Lord Parker should be passed, but he did not see fit to regard the corporation as par-

[151] 114 L. T. Rep. 1057.
[152] Ibid., 1054.
[153] Ibid., 1045.
[154] Ibid., 1055.
[155] 144 L. T. Rep. 1055

taking of the status of its shareholders. He, too, thought it fundamentally a legal device to enable incorporators to carry on business conveniently and with the benefit of limited liability. He seems to have thought that it would be unlawful to allow the representative of the Continental Company to collect money which, it was evident, was for the benefit of alien enemies and would ultimately be distributed to them.[155x] It seems certain that this conclusion could have been adequately met by the provisions of the Trading With the Enemy Act and its amendments, especially that of November 27, 1914, appointing an alien enemy property custodian. Consequently, the treatment which he thought it necessary to accord the corporate entity can hardly be said to have as great weight as the opinions of the other Lords on the point. He disposed of the whole matter by the statement that, "In my opinion, the whole discussion is solved by a very simple proposition in our law: when the object to be obtained is unlawful the indirectness of the means

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[155x] On this point Lord Shaw's opinion is decidedly more in harmony with the facts, it seems, than the Earl of Halsbury's judgment, and he at the same time accords a proper place to the separate entity. Lord Shaw says: "I do not detain your Lordships with what I think to be the extraordinary argument that if assets are realized and a business kept up, many share-holders of an English Company will, at the end of the war, be benefited. Possibly they may. It is true enough that on the other argument both they and the English share-holders might enormously suffer; so that a species of indirect pillage seems to be involved—pillage first of the enemy and secondly of English share-holders thus presumably penalized for their association with others, I must respectfully decline to admit the validity of any argument of the kind.

"I may, however, further point out that if the statute and proclamation be construed as the Court of Appeals have, I think, very rightly construed them, the results *post bellum* would be results depending upon the state of British legislation and on the terms of peace. So far as British legislation is concerned it may be mentioned that by the Act to amend the Trading with the Enemy Act of 1914, passed November 27th last, various provisions were made for the constitution of an office of custodian of enemy property. The custodian being appointed to hold such property "until the termination of the present war," and thereafter to "deal with the same in such manner as His Majesty may * * * direct." In short it seems plain * * * that the question of disposal of enemy property will be fully dealt with."—114 L. T. Rep. 1057.

by which it is to be obtained will not get rid of the unlawfulness, and in this case the object of the means adopted is to enable the thousands of pounds to be paid to the King's enemies." The judgment continues with what seems an unnecessarily extreme and doubtful conclusion as to the corporate organization, that "this machinery, while perfectly lawful in peace time, becomes absolutely unlawful when the German traders are at war with this country."

We agree with the Earl of Halsbury that, "Under these circumstances, it becomes material to consider what this thing which is described as a 'corporation' is." But we cannot at all assent to his conclusion that "it is in fact, a partnership, in all that constitutes a partnership except the names, and in some respects of the position of those whom I shall call the managing partners. No one can doubt that the names and the corporation were but the machinery by which the purpose (giving monies to the enemy) would be accomplished. The absence of the authority to issue the writ is only a part of the larger question. No one has authority to issue a writ on behalf of an alien enemy because he has no right to sue in courts of a King with whom his own Sovereign is at war. No person or any body of persons to whom attaches the disability of suing under such circumstances can have authority, and to attempt to shield the fact of giving the enemy money due to them by the machinery invented for a lawful purpose would be equivalent to enclosing the gold and attempting to excuse it by alleging that the bag containing it was of English manufacture. I observe that the Lord Chief Justice says that the company is a live thing. If it were, it would be capable of loyalty and disloyalty. But it is not; and the argument of its being incapable of being loyal or disloyal is founded on its not being 'a live thing.' Neither is the bag in my illustration 'a live thing.' And the mere machinery to do an illegal act will not purge its illegality—*trans circuitu non purgatur.*" Nor do we agree that, "After all, this is a question of ingenious words, useful for the purpose for which they were

designed, but wholly incapable of being strained to an illegal purpose. The limited liability was a very useful introduction into our system, and there was no reason why foreigners could not, while dealing honestly with us, partake of the benefits of that institution, but it seems to me too monstrous to suppose that for an unlawful, because, after a declaration of war, hostile purpose, the forms of that institution should be used, and enemies of the state, while actually at war with us, be allowed to continue in trade in an English court of justice."[156]

This seems to be an altogether inadequate treatment of the subject. It entirely disregards the fact, brought out in the other opinions, that the Trading With the Enemy Act and its amendments are wholly adequate to show lack of any possible authority in an agent after declaration of war to bring suit, without denying the validity and vitality of the separate corporate entity. Even if it had appeared that the agent did have express authority to bring such a suit by power confirmed before the outbreak of the war, the provisions of those acts adequately controlled and suspended such objectionable operation of the peace-time laws of corporate activity. Moreover, to say that no institution is a 'living' institution because it has not a human mind of its own is a confined and narrow interpretation of the term 'live' which is neither necessary nor applicable to the facts. Group will does not rest on such a determination, as I have pointed out in my discussion on that subject in the preceding chapter.[157]

Lord Parmoor was in accord with the weight of authority in his opinion that, "A company incorporated under the Companies Act has a continued existence irrespective of the shareholders for the time being on the register. It is a legal person or entity, which comprises not only those shareholders, but their predecessors and successors. It has a right to sue and a liability to be sued in the corporate name. It possesses powers and

[156] 114 L. T. Rep. 1051.
[157] See pp. 61ff, *supra*.

is subject to obligations distinct from those of the shareholders for the time being on the register acting either individually or in their collective capacity."[158] Lord Parmoor agreed with Lord Shaw that the Continental Company after the outbreak of war "does not lose the status of a company registered in this country."[159]

On the whole, Lord Parker's opinion as it appears upon the nature of the corporation is by far the most satisfactory and the most convincing. I have already quoted it [160] and it is not necessary to repeat the quotation here. One phase in particular is of great importance, for it represents a like attitude of the United States Supreme Court in the cases later discussed in this chapter, in which the court declares that it will look to the type of control of one individual, group of individuals, or corporation, over another corporation, to determine the lawfulness of the acts of the corporate entity. For this control, says the court, may raise a presumption that the acts of the corporate agents are not corporate acts—that is, done in behalf of the corporation,—or, that the corporation is the mere instrument or instrumentality of the part or of all of the individual members for the purpose of committing a fraudulent act. Lord Parker gave as "an illustration of the view which has been taken (under the Income Tax Acts, it is true) of the control which one trading company exercises over another company through the ownership of a controlling interest in the latter's shares," * * * the case of St. Louis Breweries v. Apthorpe[161] and Schonhofen Company v. Apthorpe.[162] In the latter case, in deciding that an English Company, which held a controlling interest in the shares of a United States Company, carried on business for income tax purposes in the United States by virtue of that holding and of its control over the business of the latter

[158] 114 L. T. Rep. 1062.
[159] Ibid., 1063.
[160] See pp. 101-102, *supra*.
[161] 79 L. T. Rep. 395.
[162] 80 L. T. R. 395.

company, Collins, L. J., expressly said that he was not deterred from so deciding by the decision of the House of Lords in the case of Salomon v. Salomon and Company,[163] which was so much relied on in the court below.

Speaking of the element of control, Lord Parker said, "I think this analogy not without importance." And later in his opinion appears the statement that "the enemy character of individual shareholders and their conduct may, however, be very material on the question whether the company's agents, or the persons in *de facto* control of its affairs, are in fact adhering to, taking instruction from, or acting under the control of enemies. This materially will vary with the number of shareholders who are enemies and the value of their holdings. The fact, if it be the fact, that after eliminating the enemy shareholders the number of shareholders remaining is insufficient for the purpose of holding meetings of the company or appointing directors or other officers, may well raise a presumption in this respect. For example, in the present case, even if the secretary had been fully authorized to manage the affairs of the company and to institute legal proceedings on its behalf, the fact that he held one share only out of twenty-five thousand shares, and was the only shareholder who was not an enemy, might well throw on the company the onus of proving that he was not acting under the control of, or taking his instructions from, or adhering to the King's enemies in such a manner as to impose the enemy character on the company itself. It is an *a fortiori* case," thinks Lord Parker, "when the secretary is without authority and necessarily depends for the validity of all he does, on the subsequent ratification of enemy shareholders."[164]

War conditions in England for the first time seriously have raised the challenge to the extreme doctrine of existence of the corporate entity separate and apart from the individual incorporators. In America the anti-trust prosecutions had done so

[163] 75 L. T. Rep. 426; (1897) A. C. 22.
[164] 114 L. T. Rep. 1061..

more than a generation before the World War. The association of these problems of corporate existence with the problems of trading with the enemy in war time led Lord Parker to assert that "the truth is, that considerations which govern civil liability and rights of property in time of peace, differ radically from those which govern enemy character in time of war. Joint stock enterprise and English legislation and decisions on it have developed mainly since this country was last engaged in a great European war and have taken little, if any, account of warlike conditions. The ideal joint-stock enterprise, the more unlimited the trade the better, is an ideal of profound peace. The rule against trading with the enemy is a belligerent weapon of self-protection. I think that it has to be applied to modern circumstances as we find them and not limited to applications of long ago, with as little desire to cut it down on the one hand as to extend it on the other beyond what those circumstances require."

Lord Parker came to the convincing conclusion that " a company incorporated in the United Kingdom is a legal entity, a creation of law with the status and capacity which the law confers. It is not a natural person with mind or conscience." "Such a company can only act through agents properly authorized, and so long as it is carrying on business in this country through agents so authorized and residing in this or a friendly country, it is *prima facie* to be regarded as a friend, and all his Majesty's lieges may deal with it as such." But "such a company may, however, assume enemy character. This will be the case if its agents or persons in *de facto* control of its affairs, whether authorized or not, are resident in the enemy country, or, wherever resident, are adhering to the enemy or taking instruction from or acting under the control" of enemies. A person knowingly dealing with the enemy in such a case is trading with the enemy. "The character of individual shareholders cannot of itself affect the character of the company."

In conclusion of the discussion of the Daimler case, it may be said that detailed consideration has been given it because of the keen and pertinent observations called forth by the facts before the Lords on the theories of corporate existence. In practice, the questions raised by the points involved in the case have not proved to be of great importance or difficulty since that time because many of the enemy companies registered in England have been wound up by order of the Board of Trade under the Trading With the Enemy Acts. Likewise, in the United States similar operations of the Alien Property Custodian have taken such questions out of the courts.

The Corporation Not a Citizen Within the Constitution of the United States. The early tendency of the state courts to break away from the theory of the Deveaux case as to citizenship of the corporate entity, is evidenced by the decision in Portsmouth Livery Company v. Watson,[165] in 1813. A Rhode Island corporation brought trover in a Massachusetts court. To a plea that it was not incorporated in Massachusetts, there was a demurrer. The court, in sustaining the demurrer, observed that a corporation was an artificial person whose existence was to be established like any other material fact.

A leading case in which the United States Supreme Court refuses to extend the device of looking through the corporate entity to the status of the corporators, employed by Marshall in Bank of the United States v. Deveaux, was Bank of Augusta v. Earle.[166] In that case the matter came up on writ of error to the Circuit Court of the United States for the southern district of Alabama, in an action of assumpsit on a bill of exchange, by the endorsee against the endorser. Chief Justice Taney delivered the opinion of the court. The case of the Bank of the United States v. Primrose was argued at the same time.

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[165] 10 Mass. 91.
[166] 13 Pet. 519 (1839).

D. B. Ogden, Sergeant, and Webster were counsel for the plaintiffs, and C. J. Ingersoll and Van de Gruff for the defendants. The case of New Orleans and Carrollton Railroad Company v. Earle was submitted to the court upon the arguments offered in the other two cases.

The facts admitted by the defendants were that the plaintiffs were a Georgia corporation having the power usually conferred upon banking institutions such as the purchase of bills of exchange, etc. The bill sued on was made and endorsed for the purpose of being discounted by the agent of the bank, who had funds of the bank for the purpose of purchasing bills, which were derived from bills and notes discounted in Georgia by the plaintiff bank, and payable in Mobile, Ala. The agent of the bank discounted and purchased the bill sued on in Alabama, for the benefit of his bank. The lower court found in these facts a good defence to the action. They were of the opinion that a bank incorporated by the laws of Georgia, with power, among other things, to purchase bills of exchange, could not lawfully exercise that power in the state of Alabama, and the contract for the bill was therefore void and did not bind the parties to the payment of the money. The United States Supreme Court, however, reversed the lower court, and held that, there being nothing in the constitution or laws of Alabama which enabled the court to declare that the purchase of bills of exchange in Alabama by a foreign corporation is contrary to the policy of that state, by the comity of nations a foreign corporation is allowed to make contracts within their limits, not contrary to their known policy or injurious to their interests.

To the argument that the "rules of comity do not apply to the states of the Union; that they extend to one another no rights other than those which are given by the Constitution of the United States; and that the courts of the general government are not at liberty to presume, in the absence of all legislation on the subject, that a state has adopted the comity of nations towards the other states, as a part of its jurisprudence;

or that it acknowledges any rights but those which are secured by the Constitution of the United States," the court replied that it thought otherwise. "The intimate union of these states, as members of the same great political family; the deep and vital interests which bind them so closely together, should lead us, in the absence of proof to the contrary, to presume a greater degree of comity, of friendship and kindness towards one another than we should be authorized to presume between foreign nations. * * * They are Sovereign States and the history of the past, and the events (that is, in commerce and industrial intercourse) which are daily occurring, furnish the strongest evidence that they have adopted towards each other the laws of comity in their fullest extent. * * * The silence of state authorities, while these events are passing before them, show their assent to the ordinary laws of comity which permit a corporation to make contracts in another state."

This application of the rules of international comity to the states, the court bases not wholly upon the general uses of trade, nor the silent acquiescence of the states, but upon previously decided cases cited in the argument. Such cases showed that, wherever the question had arisen, a corporation of one state had been allowed to sue in another. If it may sue, asked the court, why may it not make a contract? Just as the courts of one state took notice of the corporation so far as to allow it to maintain suit, so, said the court, there is no reason in the absence of state legislation, why one state should not recognize its existence for other purposes, as, for instance, the making of a contract. And the conclusion of the court followed this reasoning, although it did not take the occasion offered, to recognize the distinction which exists, so carefully made by Continental Jurists, between what are called civil and functional capacities of a corporation.[167]

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[167] This distinction between civil and functional capacities is designated by the term "*Rechtsfahigkeit*" and "*Zwecktatigkeit*," or "*activité juridique*" and "*activité sociale*."—See Young, Foreign Companies and Other Corporations, p. 46; Pillet, Personnes Morales en Droit Interna-

The case of Bank of Augusta v. Earle was chiefly significant because of the later influence of the dicta of Chief Justice Taney rather than the actual point decided. In the first place, the court emphatically proclaimed the constitutional power of a state to repudiate the principle of comity, and not only to refuse recognition to a foreign corporation, but to prevent it from transacting any sort of business within the state.[168] This dictum was adhered to, even after the adoption of the fourteenth amendment, and it has resulted in endless conflicts between legislatures and foreign corporations and a long course of hard-fought litigation. In the second place, the court conceded, in language that strikingly emphasized that phase of the fiction theory which turns upon the source and limitation of corporate existence as in the state of its creation, asserted the geographical theory of the non-existence of the corporation outside the boundaries of the state of its origin. This theory was to place serious difficulties in the way of suits against foreign corporations doing business in the state, and its effect was only circumvented by an artificial and cumbersome theory—an additional fiction—of implied consent to extraterritorial service. In his statement of this theory of corporate existence, Chief Justice Taney said:

"It is very true that a corporation can have no legal existence out of the boundaries of the sovereignty by which it is created. It exists only in contemplation of law, and by force of the law; and where that law ceases to operate, and is no longer obligatory, the corporation can have no legal existence. And it must dwell in the place of its creation, and cannot migrate to another sovereignty. But although it must live and have its being in that state alone, yet it does not by any means follow that its existence ever will not be recognized in other

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tional Privé, P. 96; Mamelok, Die Juristische Person Im Internationalen Privatrecht, p. 59; Henderson, The Position of Foreign Corporations in American Constitutional Law, p. 42.

[168] Henderson, Position of Foreign Corporations in American Constitutional Law, p. 49.

places; and its residence in one state creates no insuperable objection to its power to contract in another. It is, indeed, a mere artificial being, invisible and intangible, yet it is a person, for certain purposes, in contemplation of law, and has been recognized as such by the decisions of this court. It was so held in the case of United States v. Amedy, [169] and in Beaston v. The Farmers' Bank of Delaware.[170] Now, natural persons, through the intervention of agents, are continually making contracts in countries in which they do not reside; and where they are not personally present when the contract is made; and nobody has ever doubted the validity of these agreements. And what greater objection can there be to the capacity of an artificial person, by its agents, to make a contract within the scope of its limited powers, in a sovereignty in which it does not reside, provided such contracts are permitted to be made by the laws of the place?"[171]

In this statement by the court is seen the approaching conflict between the fiction of separate existence and its reality; between the language used by the court in describing the corporate entity and its actual method of treatment of it; between the restrictive view of the corporation as necessarily involving a franchise or privilege (and that of a particular state), and the normal view of a real corporate entity as a device for facilitating commercial and economic intercourse, open to all who apply under the general incorporation laws on equal terms, and no longer conveying either a special franchise or a monopoly dependent upon the necessity of a special act of the legislature.

The third dictum of Chief Justice Taney accompanied the court's rejection of Webster's argument that a foreign corporation was entitled to the protection of the privileges and immunities clause of the constitution. The court refused to extend the device employed by Marshall in Bank of the United States v. Deveaux, of looking through the corporate entity to the citizen-

[169] 11 Wheat. 412.
[170] 12 Pet. 125.
[171] 13 Pet. 588.

ship of the corporators. This position the court has ever adhered to. To it Henderson attributes "perhaps the chief cause of the anomalous constitutional status of foreign corporations today." Thirty years after the decision in Bank of Augusta v. Earle, in the case of Paul v. Virginia[172] was laid down the doctrine never since questioned, as Dr. Willoughby points out, that a corporation is not a citizen within the meaning of the term as used in the comity clause. The interstate comity clause of the federal constitution does not necessitate the recognition by the several states of corporations created by any of the other states. "Having no absolute right of recognition and enforcement of its contracts depending on their assent, it follows, as a matter of course, that such assent may be granted upon such terms and conditions as those states may think proper to impose. They may exclude the foreign corporation entirely, they may restrict its business to particular localities, or they may exact security for the performance of its contracts with other citizens as in their judgment resides in their discretion."[173]

It should be noted, however, that there are exceptions to this principle of state omnipotence when dealing with the corporations of other states. It is limited in at least three very important respects. Dr. Willoughby states it thus: "In so far as such corporations are engaged in the conduct of interstate commerce they may not be controlled, the regulation of this subject being exclusively a federal concern; they may not be deprived of property without due process of law or denied the equal protection of the laws; and the obligation of contracts entered into with them may not be impaired."[174]

In its refusal to extend the device of looking through the corporate entity to the status of the incorporators, as had been done in the Deveaux case, the court in Bank of Augusta v. Earle said that, "in that case the court confined its decision in

[172] 8 Wall. 168, 19 L. ed. 357.

[173] Willoughby, United States Constitutional Law, Vol. I, p. 219, par. 103.

[174] Willoughby, Constitutional Law, Vol. I, par. 103.

express terms, to a question of jurisdiction; to a right to sue; and evidently went even so far with some hesitation."[175] "And," said the court, "we fully assent to the propriety of that decision, and it has ever since been recognized as authority in this court.[176] But," said the court, "the principle has never been extended any further than it was caried in that case, and has never been suggested to extend to contracts made by a corporation, especially in another sovereignty." Thus the court again avowed it to be a general rule that the corporate entity does exist separate and distinct from its members. And it went on to say:

"If it [the exception to the rule, by which the separate entity is disregarded] were held to embrace contracts, and that the members of a corporation were regarded as individuals carrying on business in their corporate name, and therefore entitled to the privileges of citizens in matters of contract, it is very clear that they must at the same time take upon themselves the liabilities of citizens and be bound by their contracts in like manner. The result of this would be to make a corporation a mere partnership in business, in which each stockholder would be liable to the whole extent of his property for the debts of the corporation, and he might be sued for them in any state in which he might happen to be found." Thus was clearly indicated the disinclination of the court to disregard the corporate entity and substitute in its place, in effect, a partnership. However, while the court recognized its fictitious entity negatively to the extent that it did not look to the citizenship of the individual members of the corporation, and positively to the extent that it did recognize the existence of a corporate entity in the state of its creation, which could contract and sue and be sued in a foreign state by agent, yet it did not go so far as to accord

[175] 13 Pet. 586.

[176] The same statement is true today in the class of cases discussed later in this chapter, in which the corporate form is set up with the sole purpose of fraudulently gaining the jurisdiction of the federal courts.

citizenship to that entity, under the Comity Clause or the Fourteenth Amendment.

The precise question presented to the court in Bank of Augusta v. Earle, as distinguished from the dicta to which I have been referring, was whether the banking franchise of an Alabama state bank included the exclusive right to employ corporate capital in the purchase of bills of exchange within the state. The actual decision was that a foreign corporation could buy a bill of exchange through Alabama agents, there being no positive law or definite policy of the state against it, although it could not establish a branch bank in Alabama. This decision, however, was almost at once set at nought by the Alabama legislature.[177] The court rejected Webster's argument that a foreign corporation was entitled to the protection of the privileges and immunities clause of the United States Constitution,[178] which declared that "the citizens of each state shall be entitled to all the privileges and immunities of citizens of the several states."

In connection with our discussion of the nature of the corporation, it is of special importance to note the reasoning upon which the court based its conclusion that the corporation is not a citizen. In this case that citizenship to which, as Webster argued, a foreign corporation was entitled was not for the purpose of acquiring the jurisdiction in the federal courts nor for preventing its attachment, but it was for the purpose of gaining recognition of certain rights,—"all the privileges and immunities of citizens in the several states"—in the corporate entity itself. The court was asked to look through the corporate entity to the citizenship of the individuals,—as it had announced twenty years before that it would do, to determine the substantial nature of the parties to a suit between individuals and a corporation. But it was urged to go further, and attribute the citizenship of the individual members of the corporation to the

[177] Laws of Alabama, 1839-1840, 69.
[178] Article IV, section 2.

corporate body itself, a step which would have recognized a real separate entity to which specific rights might attach. The court, however, again acted in accord with its former interpretation of the fiction of corporate existence, and held that the entity could have no existence outside the state of its creation. At the same time it decided that by the comity of nations foreign corporations might enter into contracts in another state by agent, just as could an individual.

This, in effect, is a frank admission of the existence of a corporate entity for the particular act. In fact, the decision recognizes the existence of the corporate entity in the state of its creation, and grants to it by the comity of nations, all the benefits of actually doing business by agent in another state by its implied consent, according to the "general law and usages of trade," the "silent acquiescence of the states"—and the many cases decided in state courts * * * that a corporation of one state may sue in the courts of another.[179]

Why, then, should the courts recognize the reality, or at least the fiction of the corporate entity, so far as concerns the carrying on the corporate business within the state of incorporation, and outside of that state by agent in so far as a foreign state does not expressly deny it, while at the same time it refuses to accord citizenship to the entity and denies it reality outside of the boundaries of the state of its creation? In other words, why did the court see fit to discard its fiction, and decline to recognize the fact of corporate existence when called upon to accord to the corporate entity state citizenship under the Comity Clause and Fourteenth Amendment, while in the same decision it retained its fiction, and thereby recognized the fact of the existence of an entity within the state of its creation, with powers, within its charter limits, as great as any individual, to do business by agent outside of the state?

The answer is found in the historical and economic conditions which at this juncture brought into prominence an inter-

[179] 13 Pet. 591.

pretation of the fiction of corporate existence which had been a mere corollary involving comparatively few problems until the rapid expansion of commerce and intercourse between the states of the federal union. That part of the fiction which assumed prominence was that the corporation "is a creature of the state," and the logical deduction that, therefore, it could exist only within the state whose laws gave birth to the so-called fictitious entity.

I have quoted the words of Chief Justice Marshall in the Deveaux case, in which he stated that "our ideas of a corporation, its privileges and its disabilities, are derived entirely from the English books; we resort to them for aid, in ascertaining its character."[180] Now, England was not a federal state composed of many unit states each said to be sovereign. Hence the problems attaching to this part of the interpretation of the fiction theory were altogether problems of foreign relations, or at least relations with subjects of foreign nations. But in the United States, the case was different. The whole theory of foreign corporations was transplanted and given an artificial growth by grafting it upon interstate relations of the various states of the federal Union, in the same sense in which it had theretofore been attached to international relations—that is, the relations of states or their subjects to other sovereign nations.

A second complication increased the difficulties of corporate enterprise. Interpretation of corporate existence in old English law had always identified corporate life with privilege and special franchise. In fact, by far the greater part of early English and colonial corporate enterprise was monopolistic in character. As Henderson points out, "the monopolistic corporation was the typical one, and its prevalence gives a valuable clue to the political thought of the time with respect to corporations in general."[181]

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[180] See pp. 87ff, *supra*.

[181] Henderson, The Position of Foreign Corporations in American Constitutional Law, p. 17 ff.

In giving these corporations a place in their political philosophy, it is to be expected that the views of our forefathers should have depended somewhat on whether the particular philosopher and the persons and classes with whom his social sympathies lay, were among the beneficiaries of these valuable privileges, or were among those whose activities were restrained by them. The "insiders," on the one hand, drew their inspiration from the century-long struggle between the English boroughs and the king and feudal barons, and more immediately from the struggle for charter rights and privileges between the colonies and the king. These struggles had come to invest such terms as "liberties," "privileges," "immunities," "franchises," the stock terms found in all corporate charters, with a peculiar sanctity, as things they and their forefathers had fought and bled for.[182] On the other hand, as Henderson suggests, the "outsiders" relied on the powerful appeal of the philosophy of natural law, claiming rights not from any charter or sovereign grant, but from the inherent nature of man.[183]

This conflict between the philosophy of liberties, privileges, and immunities, and the philosophy of natural rights, was an ever-present and insistent one at the Philadelphia Congress in 1774.[184] Mr. John P. Davis, in his treatise on corporations,[185] calls attention to the monopolistic character of the early continental corporations. He says the "departure from the feudal

[182] See the samples of Charters of Liberties reprinted in Messrs. Bland, Brown & Tawney's English Economic History, Select Documents, 116 ff.

[183] See the illuminating protest to the English Parliament, against commercial monopolies, in 1604,—Journals of the House of Commons, I, 218. First among the objections is the following: "Natural Right: —All free subjects are born inheritable, as to their land, so also to the free exercise of their industry in those trades, whereto they apply themselves and whereby they are to live. Merchandise being the chief and richest of all others, and of greater extent and importance than all the rest, it is against the natural right and liberty of the subjects of England to restrain it into the hands of some few, as it now is."—Henderson, Position of Foreign Corporations, etc., p. 17.

[184] See John Adams, Diary, Works, II, 370.

[185] Vol. II, 241.

system, it is hardly necessary to suggest, was accomplished largely through a chaotic mass of exemptions of subjects from feudal obligations. The unevenness of the development of exemptions, combined with the inability of the state to absorb political powers lost by the feudal nobility—in other words, its inability to substitute, until after centuries of development, a national state for an aggregate of feudal manors—left here and there bunches of political powers vested in communities that were afterward viewed as technical corporations. The work of the English law, during the twelfth and thirteenth and fourteenth centuries, as far as the promotion of liberty was concerned, was largely to construe and enforce the mass of exemptions. The jurist comprehended the nature of individual rights and obligations by comparing them or contrasting them with normal rights under the decaying feudalism; from that point of view all, or nearly all, individual rights and obligations were in a sense exceptional." But the exception became the rule when by the passing away of feudalism the system of law reached the level of the individual and interpreted his rights and obligations directly rather than by contrasting them with a prior status, even though it continued to use in describing them the absolute terminology of feudalism. The communities to which clusters of powers had been transferred were now compared, not with the feudal lords, by whom the powers had been conceded, but with the normal English subject.

I have quoted these statements at some length, to show that the "identification of incorporation with the grant of special and exclusive privileges or monopolies, and the fear that the corporation would infringe on the 'natural rights' of citizens, was the chief source of the early opposition to corporations."[186] Add to this the inherent economic jealousies and fears which characterized the attitude of the states towards each other before, and for three-quarters of a century after, the formation of the Union, and it is not difficult to see why, to persons who thus

[186] Henderson, Position of Foreign Corporations, etc., p. 19.

identified with monopoly and exclusive franchise the law of foreign corporations, that law as it had appeared in England was accepted with open arms. For, as Henderson points out, it hardly needed argument that one sovereign could not give a monopoly in the territory of another sovereign, and as long as these corporate monopolies were looked upon with such jealous eyes, their power rigidly confined to what the charter expressed, and its language strictly construed against them, international comity could hardly expect the courts of the foreign sovereiggn to admit them without express legislative mandate.

Even today the results of the emphasis of this side of the fiction theory of corporate existence is given expression to, in the reiteration of such terms as those which have sprung from Chief Justice Marshall's words in the Deveaux and Dartmouth College cases, born of the monopolistic conception and absolutely unfit to meet the facts of industrial and commercial corporate existence under the general laws.[187] Corporate existence, said those courts, is a "privilege," a "franchise," whose exercise will be regarded with a jealous eye; for the corporation is a "mere creature of the state."

Out of the varying interpretations placed upon this side of the fiction of corporate existence, the courts and legists have evolved two opposing theories of the nature and status of corporations which have carried their activities into another sovereignity from that in which their charter was secured. Henderson describes the first theory as that which "tends to repel the corporation, to subject its activities within a state to peculiar burdens and restrictions, even to deny that they have corporate existence. The other theory welcomes them, places their property and their activities under the protection of international

[187] Such, for instance, is the very positive opinion of Joseph C. France, Esquire, author of Principles of Corporation Law, and general counsel of the United Railways and Electric Company, Baltimore. Mr. France acted as secretary to the committee appointed by Governor Smith of Maryland to draft a revision of the Maryland Corporation Laws, enacted in 1908.

or constitutional law, and accords them a position of equality with domestic corporations. The two theories have their roots in divergent conceptions of the nature of corporations.[188] The restrictive theory tends to emphasize the extraordinary character of the privileges with which the members of a corporation are endowed, and the high nature of the act of sovereignty of which their corporate franchise is conceded. The liberal theory is largely an evolution of the last generation, and looks upon the corporation rather as a normal business unit, and its legal personality as primarily a convenient mechanism of commerce and industry." The restrictive theory is the one assumed by the court in the case of Bank of Augusta v. Earle.

It seems inevitable that the denial of citizenship to corporations within the meaning of the Comity Clause and the Fourteenth Amendment will be abandoned at some time in the future. It is true that the doctrine of Paul v. Virginia[189] has been adopted as sound by the federal courts.[190] And by that doctrine it is held that corporations are not citizens within the meaning of that clause of the United States Constitution; that provision applies only to natural persons, members of the body politic, owing allegiance to the state, and not at all to "artificial beings created by the legislature, and possessing only the attributes with which they have been endowed by the legislature." This same doctrine has been applied to the interpretation of the Fourteenth Amendment to the Constitution, which forbids the states to "make or enforce any law abridging the privileges or immunities of citizens of the United States."[191]

But, as Henderson says, "whatever a system of law may say about it, in fact, a group engaged in a co-operative undertaking has common, group interests. It is fact, not fiction. To pro-

[188] See E. Hilton Young, Foreign and Other Corporations, Cambridge (Eng.) Univ. Press, 1912; and Henderson, Position of Foreign Corporations, etc., Chapter I.

[189] 8 Wall, 168; 19 L. ed. 357.

[190] See citations in 60 L. R. A. 330, Note.

[191] Insurance Company v. New Orleans, 1 Woods, 85, Federal Case No. 7,052.

tect those interests the group has acquired a set of legal rights and powers and privileges which has been denominated legal personality."[192] And, as to the recognition of citizenship in the privileges and immunities clauses of the fourth and fifth amendments and the fourteenth amendment and article four of the constitution, it is true that not everything which a state could see fit to call a corporation must be deemed a citizen. There must be the human substratum, the group whose interests the legal personality protects. This is the substance to which the policy of the constitutional clause attaches. "Once this substance is recognized, there is nothing in the form of the legal entity to render the word 'citizen' inapplicable."[193]

For purposes of jurisdiction, as has been seen, "a corporation is now to all intents and purposes a citizen of the state in which it is domiciled. This must be frankly recognized; to retain the fictitious presumption that all its stockholders are citizens of that state would be to leave a serious blemish on our constitutional system. In fact, more often than not, the fiction has been tacitly abandoned, and the corporation referred to as itself a citizen for jurisdictional purposes.[194] To continue to force precedent, that the courts can supply what they consider a consider a constitutional defect by presuming a fact which they know to be untrue, would be a standing invitation to judicial usurpation. * * * Moreover, if we look at the scheme of the constitution as a whole, there is little doubt that the word 'citizen' was used in precisely the same sense in the jurisdictional provisions as in the privileges and immunities clause."[195] The "doctrine of indispensable citizenship is not a mere procedural

[192] Henderson, Position of Foreign Corporations, etc., p. 176.
[193] Henderson, p. 180.
[194] Insurance Co. v. Francis, 11 Wall. 210, 216 (1870); *Ex parte* Schollenberger, 96 U. S. 369, 377 (1877); Railroad Co. v. Koonly, 104 U. S. 3 (1881); Goodlett v. Rd. Co., 122 U. S. 391 (1887); Nashua & Lowell Rd. v. Boston & Lowell Rd., 136 U. S. 356, 372 (1890); Martinez v. Association de Senoras, 213 U. S. 20 (1909), Shulthis v. McDougal, 225 U. S. 561 (1912).
[195] Henderson, pp. 181, 182.

fiction, for it confers substantial rights, and results in important limitations on the legislative powers of the state." For the state, according to the Supreme Court, cannot either directly or by threat of expulsion or indictment, prevent a corporation from asserting its right in the federal courts.[196]

Partnership Liability of Stockholders. This discussion of the denial of corporate existence to foreign corporations outside the state of their creation raises the question as to how far and under what conditions the individual incorporators will be treated as partners and incur partnership liability in cases where the state does not recognize the right of the corporation to do business within its limits. The findings by the courts depend, on the one hand, upon whether the corporation is regularly organized in the state of its origin, or defectively or illegally organized;[197] and, on the other hand, whether liability attaches merely by reason of being a stockholder in the miscreant corporation, or must depend upon active participation of the corporators in the business of the corporation carried on in the foreign jurisdiction. There is a class of cases, for instance, in which it is attempted to question the compliance of a foreign corporations with the laws of the state of its creation in a suit against some members in another state. When the corporation does not appear to have been doing business in the state of the forum, this class of cases is excluded.

It is the theory of some early cases that an act of incorporation can have no extraterritorial effect.[198] Accordingly, incorporation in a foreign state is no protection against liability arising from the manner in which a group of persons are doing

[196] Western Union Telegraph Company v. Frear, 216 Fed. 199 (1914), affirmed on a different principle in 241 U. S. 329 (1916). Herndon v. Chicago, Rock Island and Pacific Railway, 218 U. S. 135 (1910). Donald v. Philadelphia and Reading Coal Company, 241 U. S. 329 (1916).

[197] Rutherford v. Hill, 22 Ore. 218, 17 L. R. A. 549; Swofford Bros. Dry Goods Company v. Owen, 37 Okla. 616. L. R. A. 1916-C, 196.

[198] Taylor v. Branham (1895), 35 Fla. 297, 39 L. R. A. 362.

business; if they are doing business as a partnership, a partnership liability arises. But this doctrine has not been generally accepted, because the relation existing between the states is such as to make it impracticable. Hence the weakening of the restrictive theory of the corporate entity with the resultant precarious position of the fiction theory as to the nature of the entity and the strengthening of the realist conception. One state is bound to recognize a corporation formed in another state.[199] Accordingly, where a corporation is regularly formed in one state, its stockholders cannot be held liable as partners where it has been carrying on business in another state.[200] By the weight of authority, the failure of a foreign corporation to comply with the laws of the state in which it is doing business relative to foreign corporations, does not render the stockholders liable as partners.[201] This is in harmony with the inevitable tendency to accord reality to the corporate entity, with an increasingly small number of exceptions.

Corporations as Persons Within the United States Constitution. Corporations have been discussed in relation to the possibility of their being considered as citizens within the United States Constitution. It is now proposed to ask how far they are treated as "persons" within the terms of that instrument.

It is a general rule of the state courts that the term "person," used in a statute, includes corporation unless there is something in the law showing the legislative intention to restrict its application.[202] It has been shown that the corporation is accorded citizenship, in effect, within article three, section two of the United States Constitution, in cases of federal jurisdiction over

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[199] Merrick v. Van Santvoord, cited in annotation on Partnership Liability of Stockholders of a Foreign Corporation in a State (New York) in which it is doing business, L. R. A. 1917-B, 576.

[200] Boyington v. Van Etten (1896), 62 Ark. 63, 35 S. W. 622.

[201] Note, L. R. A. 1917-B, 576.

[202] Crafford v. Warwick Co. Supervisors, 87 Va. 110, 12 S. E. 147.

disputes between parties of diverse citizenship; that this was, however, regarded by the courts as an exception to the rule of the fiction theory that the courts will not look beyond the corporate form to the individual members of the corporation; and that it has been in effect abandoned by the introduction of another fiction in the form of the conclusive presumption that all the members of the corporation are citizens of the state of incorporation and therefore the citizenship of the corporation for purposes of suit in the federal courts is considered to be that of the incorporators—that is, the state which issued the charter. It has also been pointed out that the courts have not gone so far in the matter of attributing citizenship to a corporation for the purposes of guaranteeing it immunities and privileges under the comity clause, nor has it been accorded such citizenship within the meaning of the clause of the fourteenth amendment forbidding states to make or enforce any law abridging the privileges or immunities of citizens of the United States.

The status of foreign corporations, however, shows that this fictitious attribution of citizenship for purposes of suit, and the denial of citizenship under the comity clause and the fourteenth amendment, both stand upon the old theory which recognizes the existence of the separate-corporate entity in fiction only, and not fact. Activities of foreign corporations, however, and the status accorded them as existing in the state of their creation, and capable of action by agent in a foreign state by implied or express consent of that state, bears witness to the recognition of the reality of the separate entity, guarded, to be sure, at times, by the court's assumption of a fiction, made necessary by the pressure of the facts of industrial and commercial intercourse.

Denial of citizenship, however, is denial of only one capacity in the corporate entity, as in an individual person. It was pointed out in the discussion of the Deveaux case, that the court recognized that the corporation might be an "inhabitant or occu-

pier," within the meaning of certain statutes. The question now arises, to what extent is the corporation to be regarded as a "person" within the provisions of the United States Constitution? We find that the Supreme Court of the United States, while denying citizenship to the corporation under the fourteenth amendment, accords it the right to be considered as a person to whom the states are not at liberty to deny the equal protection of the laws.[203] Although this proposition has not been accorded unreserved recognition, it is now well settled. I shall not discuss the various changes of opinion indicated by the different court decisions, but simply note the condition of the law and its underlying theories as they exist today. The economic reason for holding the corporation to be a person within the fourteenth amendment's provision prohibiting states from depriving any person within their jurisdiction of equal protection of the laws, was a logical necessity, in order that the corporation might be entitled to equal protection in respect of the burdens of taxation. For the courts generally held corporations to be persons within the taxing statutes. Taxation laws, as it will be remembered from the discussion of the English cases, in which the corporation was held to be an "inhabitant" or "occupier," deal with residents, inhabitants, or occupiers of land, rather than with citizens.[204]

The question of whether the corporation is to be included under the terms of the fourth and fifth amendments to the constitution came before the United States Supreme Court in the case of Hale v. Henkel.[205] In that case it was decided that the corporation was not to be considered to be a person within the meaning of the fifth amendment where the facts involved a prosecution under the Sherman Act, even though, by the express

[203] Santa Clara County v. Southern Pacific Railroad Co., 118 U. S. 394, 30 L. ed. 118; Gulf, C. & S. F. R. Co. v. Ellis, 165 U. S. 150, 41 L. ed. 666.

[204] Tripp v. Merchants Mutual Fire Insurance Company, 12 R. I. 435; *Ex Rel.* Thurber-Whyland Co. v. Barber, 141 N. Y. 118, 23 L. R. A. 95.

[205] 201 U. S. 43.

provisions of section eight of that Act, corporations are deemed to be persons.

The search and seizure clause of the fourth amendment to the United States Constitution provides that "the right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no warrants shall issue, but upon probable cause, supported by oath or affirmation, and particularly describing the place to be searched and the persons or things to be seized." The court's decision, however, as to the application of the fourth amendment, did not turn upon the interpretation of the word "person." This clause, said the court, was not intended to interfere with the power of the courts to compel the production, upon a trial, of documentary evidence. "Having already held that by reason of the immunity act of 1903 the witness could not avail himself of the fifth amendment, it follows that he cannot set up that amendment as against the production of the books and papers, since in respect to these he would also be protected by the immunity. We think it quite clear that the search and seizure clause of the fourth amendment was not intended to interfere with the power of courts to compel, through a *subpœna duces tecum,* the production, upon a trial in court, of documentary evidence." This statement of the court, it will be observed, did not refer to corporations any more or on any different grounds than individuals. Hence this case cannot be taken as one in which the term "person" has a different content when applied to corporations than when applied to persons. Its significance lies in the fact that it places the corporation in a different position than the individual under the immunities clause of the fifth amendment.

The fifth amendment provides, among other things, that "no person * * * shall be compelled in any criminal case to be a witness against himself." It was urged by Mr. Henry W. Tuft, Special Assistant to the Attorney General, that the protection of the fourth and fifth amendments is based alone upon the personal privilege of the witness. The objections urged by the

witness in this case could not, it was urged, be relied upon for the benefit of the corporation of which he was an officer, and if the privilege could not be asserted under the fifth amendment, it was urged that it was plain it could not be so invoked under the fourth amendment. The court upheld the argument against the application of the clause of the fifth amendment to corporations. It based its decision upon the nature of the corporation and the object of the Sherman Act. While an individual may, it said, lawfully refuse to answer incriminating questions unless protected by an immunity statute,[206] a corporation is a creature of the state, and there is a reserved right in the legislature to investigate its contracts to find out whether it has exceeded its powers. It was insisted in the argument to the court that, while the immunity statute may protect individual witnesses, it would not protect the corporation of which the appellant was the agent and representative. "This is true," said the court, "but the answer is that it was not designed to do so. The right of a person under the fifth amendment to refuse to incriminate himself is purely a personal privilege of the witness. It was never intended to permit him to plead the fact that some third person might be incriminated by his testimony, even though he were the agent of such person." This statement by the court is of tremendous importance when it is considered that the corporation, by its very nature, can act only by agents. The logical conclusion from the court's interpretation seems, therefore, to be not necessarily that the corporation cannot be considered as a person within the meaning of the fifth amendment, but that, because of the fact that it is always necessary for the corporation to act by agent, and the fifth amendment is not broad enough to include such a contingency, therefore, the corporation is to be excluded from the protection of that clause of the United States Constitution.

The result is that the corporation is said not to be included within the provision of the fifth amendment, not by reason of

[206] 32 Stat. 854, 904, for instance.

any theory of corporate existence or any fiction of the nature of the corporation, but because no person can enjoy the protection of the fifth amendment by agent. It acts only directly upon the person. Since the corporation cannot act except through an agent, it is barred from asserting the protection of the amendment. This certainly does not seem to be in accord with a just treatment of the facts, and it is suggested that in the future the court may have occasion to give the matter a broader interpretation, just as it found necessity, for purposes of taxation, to treat in a broader way the provision for equal protection of the laws in the fourteenth amendment.

The present position of the court on this matter may be further appreciated by a more extended quotation from the opinion. Continuing from the above quotation, Mr. Justice Brown said: "A privilege so extensive might be used to put a stop to the examination of every witness who was called upon to testify before the grand jury with regard to the doings or business of his principal, whether such principal were an individual or a corporation. The question whether a corporation is a 'person' within the meaning of this amendment really does not arise, except, perhaps, where a corporation is called upon to answer a bill of discovery, since it can only be heard by oral evidence in the person of some one of its agents or employees. The amendment is limited to a person who shall be compelled in a criminal case to be a witness against himself, and if he cannot set up the privilege of a third person, he certainly cannot set up the privilege of a corporation. As the combination or conspiracies provided against by the Sherman Anti-Trust Act can ordinarily be proved only by the testimony of parties thereto, in the person of their agents or employees, the privilege claimed would practically nullify the whole act of Congress. Of what use would it be for the legislature to declare these combinations unlawful if the judicial power may close the door of access to every available source of information upon the subject? Indeed so strict is the rule that the privilege is a personal one that it has been held in some cases that counsel

will not be allowed to make the objection. We hold that the questions should have been answered."[207]

The practical requirements of the rules of evidence, therefore, actuated the court narrowly to construe the word "person" in this case. Its decision did not rest primarily upon any theory of the nature of the corporation or of corporate existence, as the above quotation shows. But the court did go on to say[208] that, "conceding that the witness was an officer of the corporation under investigation, and that he was entitled to assert the rights of the corporation with respect to the protection of its books and papers, we are of the opinion that there is a clear distinction in this particular between an individual and a corporation, and that the latter has no right to refuse to submit its books and papers for an examination at the suit of the state. The individual may stand upon his constitutional rights as a citizen. He is entitled to carry on his private business in his own way. His power to contract is unlimited. He owes no duty to the state or to his neighbors to divulge his business or to open his doors to an investigation so far as it may tend to incriminate him. He owes no such duty to the state, since he receives nothing therefrom, beyond the protection of his life and property. His rights are such as existed by the law of the land long antecedent to the organization of the state, and can only be taken from him by due process of law, and in accordance with the constitution. * * * Upon the other hand, the corporation is a creature of the state. It is presumed to be incorporated for the benefit of the public. It receives certain special privileges and franchises, and holds them subject to the laws of the state and the limitations of its charter. Its powers are limited by law. It can make no contract not authorized by its charter. Its rights to act as a corporation are only preserved to it so long as it obeys the laws of its creation. There is," the court concluded, "a reserved right in the legislature to

[207] 201 U. S. 70.
[208] 201 U. S. 74.

investigate its contracts and find out whether it has exceeded its powers." For, said the court, "it would be a strange anomaly, to hold that a state having chartered a corporation to make use of certain franchises, could not in the exercise of its sovereignty inquire how these franchises had been employed, and whether they had been abused, and demand the production of the corporate books and papers for that purpose. The defense amounts to this: that an officer of a corporation, which is charged with a criminal violation of the statute, may plead the criminality of such corporation as a refusal to produce its books. To state this proposition is to answer it. While an individual may lawfully refuse to answer incriminating questions unless protected by an immunity statute, it does not follow that a corporation, vested with such privileges and franchises, may refuse to show its hand when charged with an abuse of such privileges."

Now, it is submitted that this doctrine set forth by the courts as to the special privileges and franchises of the corporation and the presumption that it is presumed to be incorporated for the benefit of the public, is a relic of the old concepts of corporate existence which grew up prior to the period of the development of the industrial corporation of the nineteenth century, and is inapplicable to them. The case presents a typical example of facts pointed out in the discussion above, as to the sources of our concepts of the nature of the corporation and the resultant foundation in history rather than in reason, of the idea which regards the existence of a corporation as a privilege or franchise to be watched and guarded with jealousy by the state which granted it power, rather than as an ordinary convenient device for the purpose of carrying on joint business enterprises, and open, under general incorporation laws, to all persons alike who wish to take advantage of them. This is not a case involving a public corporation, nor even a public-service corporation. Nor is it one which presents the aspect of a private corporation endowed with a monopolistic franchise by the state, such as those that characterized the monopolistic era of cor-

porate existence during the period from the twelfth to the nineteenth centuries. The case of Hale v. Henkel presented the aspect of two private business corporations, the MacAndrews and Forbes Company and the American Tobacco Company, charged with violation of the Sherman Anti-Trust Act. Doubtless the decision of the court was a just one, but it is to be deplored that the attenuated doctrines of an age gone by, which knew practically no private industrial corporations, should be thus perpetuated by dicta of the court as to outworn theories of corporate existence.

CHAPTER V.

THE EXTENT TO WHICH THE COURTS DISREGARD THE CORPORATE ENTITY.

The Fiction Theory of Separate Existence Disregarded to Prevent Fraud. There is, in addition to those cases involving questions of federal jurisdiction, a class of cases in which the fiction theory of the separate existence of the corporate entity, as well as the irrebuttable presumption as to corporate citizenship for jurisdictional purposes, yields to the equitable dotrine of fraud. When, by considering all of the circumstances presented in the evidence, the courts find that a corporation has been brought into being or utilized for the sole purpose of enabling the incorporators to bring a suit in the federal courts by reason of diversity of citizenship between the corporation and other parties to an intended suit, where the corporators could not have the benefit of the federal jurisdiction on this ground in their individual capacities, the court, for the purpose of determining the real parties to the suit, looks beyond the separate corporate entity. It inquires as to the intent of the incorporators in bringing it into existence. If it finds that the corporation is the mere agent of the incorporators for this particular purpose, it declines to hold that the corporate entity is the real party to the suit.

These cases do not deny the existence of the corporate entity. The entity itself is not declared to be illegal or non-existent. But they do hold that the corporate entity is not the real party to the suit, and that it is an attempted fraud upon the federal courts to thus essay to do by indirection what the individual incorporators could not do directly.

So far as the fiction theory of corporate existence is concerned, it should be noted that we are here approaching it again

from a different viewpoint. The Deveaux case had taken the ground that, for the purposes of allowing the parties to a suit to bring their case into a federal court where they might do so in their individual capacities on account of diversity of state citizenship, the court would look through the separate corporate entity to the individuals and entertain suit by the corporation on the ground that the corporators were the real parties. In the case of Bank of Augusta v. Earle, the court's action in the Deveaux case was said to be exceptional and applicable only to questions determinative of the jurisdiction of the federal courts. In the later modifications of this view in Louisville, Cincinnati and Charleston Railroad v. Leston, and Ohio and Mississippi Railroad v. Wheeler, the separate entity of the corporation was recognized. The court still kept up the appearance of looking through the corporate entity to determine the citizenship of the individual members and thereby decide whether or not jurisdiction would attach. But in order to do so it had to introduce the pure fiction that all individual members are citizens of the state in which alone the corporation has been given legal birth, and that a suit by or against the corporation in its corporate name must be irrebuttably presumed to be a suit by or against citizens of the state which created the corporate body. This absurd fiction as to the citizenship of the individual members of a corporation is made necessary by the court's action in the Deveaux case disregarding its own well-established fiction of separate corporate existence.

Thus, one fiction had to be set up to meet a special case because of the abandonment of another fiction in an exceptional case. This exceptional abandonment the court thought necessary because, by its interpretation of the term "citizen" in Article three of the United States Constitution, citizenship was confined to individual persons. That that conception sprang from an interpretation of the nature of a corporation which had its source in fiction and attained its object by franchised monopoly, makes it entirely inapplicable to the private indus-

trial corporation of today. Abandonment of the exceptional disregarding the separate corporate entity in cases in which it is sought to determine the jurisdiction of federal courts, and a frank recognition of the separate entity as capable of itself being a citizen within the meaning of the United States Constitution, would do away with both the confusing fiction as to citizenship and the exceptions to the fiction of separate corporate existence. This would entirely eliminate one fiction from the law and discard an exception to another. The clear organization of concepts of the law in an ordered system would be attained to better advantage.

So long as the present doctrine of looking through the corporate entity to the individuals that compose it is a part of our law, however, it should be kept in mind that it is an exception to the general theory of separate corporate existence. The fiction as to the irrebuttable citizenship of the members is an exception to an exception. Hence we are not surprised to see the courts abandon this doubly exceptional fiction when it is urged for a purpose not intended—that is, to commit fraud.

This is set forth in a line of cases which deal with attempts to obtain the benefit of federal jurisdiction by use of a corporation, as the courts say, fraudulently. For example, an individual or a number of individuals in one state wish to bring an action against other individuals of the same state. For some reason they do not wish to bring the suit in the state courts, but desire it to be heard in the federal tribunal. Unless there is some ground upon which the United States Constitution and statutes permit them to bring their suit in its courts, they cannot do so. There may be nothing in the nature of the subject-matter of suit which would give this right. Therefore, they conceive the idea of creating a corporation in another state, to which they may transfer the property and right of action. Such a corporation, by the doubly exceptional fiction referred to above, will be conclusively presumed to be made up of citizens of the state of incorporation. By a logical deduction, therefore, from the court's own fiction a situation has been created in which

there is the requisite diversity of citizenship in the presence of which jurisdiction may attach.

The United States Supreme Court, however, in this proceeding sees an attempted fraud upon the federal courts. It therefore abandons its fiction so forcibly laid down by Chief Justice Taney in Ohio and Mississippi Railroad Company v. Wheeler[209] and by Justice Wayne in Louisville and Nashville Railroad road Company v. Leston, that "a corporation created by and transacting business in a state, is to be deemed an inhabitant of the state, capable of being treated as a citizen for all purposes of suing and being sued, and an averment of facts of its creation and the place of transacting business is sufficient to give the circuit court jurisdiction."[210]

Miller and Lux, Incorporated, v. East Side Canal and Irrigation Company,[211] is a case in point. Miller and Lux, Incorporated, was organized as a corporation in Nevada, but was to act only as an agent of Miller and Lux, a corporation of California. The California corporation was the owner of all the capital stock of Miller and Lux, Incorporated, which, as a corporation, had no existence except as a mere agent of Miller and Lux. Justice Harlan, delivering the opinion of the court, said: "The agreement that all the property of the California corporation should be transfered to the Nevada corporation was attended by the condition that all the capital stock of the new corporation should be issued to the California corporation which remained in existence with full power as the owner of such stock to control the operations of the Nevada corporation."

This case clearly illustrates the vitality of the doctrine of agency in determining the extent to which the courts will disregard the plea of separate entity, when the corporation has been brought into legal existence in full compliance with the conditions imposed by the state in which it was created. If it is

[209] 1 Black, 286, 296.
[210] 2 How. 497.
[211] 211 U. S. 293 (1908),—a case which came up from the circuit court of the southern district of California.

sought to accomplish illegal purposes through a corporation, the corporate body will not blind the eyes of the courts to the attempt to use it unlawfully as an agent. The court indicates as follows what, in its mind, may be accepted as evidence that the agency is at an end: "If before the institution of this suit the California corporation had distributed among those entitled to it the stock of the Nevada corporation, issued to it as fully paid up stock, and had then ceased to exist or been dissolved, a different question might have been presented, but such is not this case." "As the facts were, when this suit was brought the California corporation could at any time, even after this suit was concluded, have required the Nevada corporation, without any new or valuable consideration, to surrender all of its interest in the property which it had obtained from the California corporation for the purpose of acquiring a standing in the circuit court of the United States. In other words, the Nevada corporation had no real interest in the property." Such a state of facts the court found to be "collusive and fraudulent."

Speaking of the Act of 1875,[212] Mr. Justice Harlan said: "This was for the protection of the court as well as the parties against frauds upon its jurisdiction. * * * As was very properly said by Mr. Justice Miller, speaking for the court in Barney v. Baltimore, [213] such transactions for such purposes are frauds upon the court and nothing more."

This question of fraud upon the jurisdiction of the federal courts had been raised in Lehigh Mining and Manufacturing

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[212] 18 Stat. at Large, 470, 472, Chap. 137; U. S. Comp. Stat., 1901, pp. 508, 511, par. 5. "If at any time after a suit is commenced in a Circuit Court of the United States it shall appear to the satisfaction of the court that such suit does not really and substantially involve a dispute or controversy, properly in the jurisdiction of said Circuit Court, or that the parties to said suit have been improperly or collusively made or joined, as plaintiffs, or defendants, for the purpose of creating a case cognizable or removable under this act, the said Circuit Court shall proceed no further therein, but shall dismiss the suit or remand it to the court from which it was removed, as justice may require."

[213] 6 Wallace, 280, 288.

Company v. Kelly.[214] In that case Justice Harlan read into the law, as stated in the Leston case, the inference that the averment of the facts of the organization and place of transacting business is not sufficient; but, where the fraudulent intent of its organizers is charged, cause must be shown why separate corporate existence should not be disregarded when it is impossible to divorce the fraudulent intent of individual incorporators from the intent of the corporation itself. Although the Act of 1875 had been passed since the decision by the court in the Leston case, Justice Taney held that not this law alone, but older general principles of previously decided cases controlled.

For instance, an examination of the opinion in Barney v. Baltimore shows that there is nothing peculiar to the corporate entity which induces the court to invoke this rule, for the same rule was applied where the person to whom the property was conveyed for purposes of gaining federal jurisdiction was a "natural" instead of an "artificial" person. The court, in the Miller case, after citing Barney v. Baltimore, said: "We do not intend by what has been said to qualify the general rule, long established, that the jurisdiction of a circuit court, when based on diversity of citizenship, cannot be granted upon the ground merely that the party's motives in acquiring citizenship in the state in which he sues was to invoke the jurisdiction of a federal court. But that rule is attended by the condition that the acquisition of such citizenship is real, with the purpose to establish a permanent domicile in the state of which he professes to be a citizen at the time of suit, and not fictitious or pretended."

This is a very significant statement. It throws new light on the attitude of the courts towards the separate corporate entity. It indicates that they are not reverting to the position taken in Bank of the United States v. Deveaux. The court did not abandon the rule in the Leston case. It did not deny that a corporation as such was to be regarded as a separate entity, nor that that entity might be regarded as having a citizenship for the

[214] 160 U. S. 327 (1895).

purpose of suit in the federal courts. What the court did decide was that such citizenship must be real, and that the court would not hold it to be real unless the corporation was created with the purpose of establishing a permanent domicile in the state of which it proposed to be a citizen.[215]

A third and the latest case in this line of decisions is that of the Southern Realty Investment Company v. Walker.[216] In even more positive language than before, the court, again speaking through Justice Harlan, denied jurisdiction, and held the corporate entity to be the mere agent of the individual persons in another state for the purpose of attempting to commit fraud upon the court. It was said: "There was evidence leading to the conclusion that the Southern Realty Investment Company was brought into existence as a corporation only that its name might be used in having controversies that were really between citizens of Georgia determined in the federal rather than in the state court. It did not, however, have, and was not expected to have as a corporation any will of its own or any real interest in the property that stood or was placed in its name. It was completely dominated by two Georgia attorneys, who secured its incorporation under the laws of South Dakota through the agency of a South Dakota lawyer, who, in a letter to one of the Georgia attorneys, claimed that his office had within three years secured nine hundred and eighty-five charters under the laws of that state for non-residents and part of its busines was to 'furnish' South Dakota incorporators, when necessary, with dummy directors."

In short, said the court, "the plaintiff company was and is merely the agent of the Georgia attorneys, who brought it into existence as a corporation that individual citizens of Georgia,

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[215] As to the attitude of the courts upon the significance of "intent" and "motive" in determining the agency, see, in addition to Miller and Lux, inc., v. East Side Canal and Irrigation Co. (1908), 211 U. S. 293, 297, United States v. Milwaukee Refrigerator Co., 142 Fed. 247, and 4 Wash. C. C. 101, 103 (Washington, J.).

[216] 211 U. S. 603 (Error to C. C., S. D., Georgia).

having controversies with other individual citizens of that state, might, in their discretion, have the use of its corporate name in order to create cases applicable within the jurisdiction of the federal court. It had, it is true, a president and a board of directors—all of whom were citizens of Georgia—two of the five directors being Georgia attorneys, and one being the female stenographer of such attorneys—but the president and a majority of the directors were the holders of only one share of donated stock and recognized it to be their duty to represent the Georgia attorneys and to obey, as they did obey, their will implicitly. The company, in respect of all its business, was the agent of those attorneys, to do their bidding. Its president testified that he did not know for what purpose the company was really organized, or that it had ever done any business except" as to the prosecution of these suits, "or that it had any money. Its place of business in Georgia was in the office of the Georgia attorneys. Its pretended place of business in South Dakota was in what is called a domiciliary office, maintained by the attorney in that state who procured its charter. The company's president never knew of its doing any business in South Dakota.

"As a corporation the Southern Realty Company may be deemed a mere sham. It has, in fact, no property or money really its own, and it was not intended by those who organized it that it should become a real owner of any property of its own in South Dakota or elsewhere."[216x]

These decisions have been set forth at some length because they plainly show that one clear case in which the courts will disregard the fiction of separate corporate existence is under circumstances of attempted fraud upon the jurisdiction of federal courts. But the position of the court is not wholly clear. In the first place, it should be remembered that these cases are not to be taken as precedents for a general doctrine that the courts will disregard the theory of the separate existence of the corporate entity and deal with the persons composing the corpora-

[216x] 211 U. S. 606.

tion. The court is acting in a strictly confined and specialized field: that of jurisdictional disputes. These represent exceptional situations in Anglo-American law, and especially in the United States where the constitution introduces special rules of interpretation. To be sure, these have been largely overcome by the fiction of an irrebuttable presumption of citizenship and the doctrine of the Leston case, but the Lehigh case as well as the Miller and Lux case showed that the court regarded it as perfectly possible for the corporate entity to attain a domicile in a state other than that in which its incorporators were domiciled, and that quite as much as any natural person. The court did not deny the capacity of the corporation to attain a valid citizenship for the purposes of suit, but it said that such a citizenship would not be in fact attained unless there was a concomitant purpose to establish a permanent domicile.

Agency as a Ground for Disregarding the Separate Entity. In all of these cases, but especially in Southern Realty Company v. Walker, it is asserted that the corporation was the mere agent of its creators, in an attempted perpetration of fraud. Although an act of Congress is used to strengthen the court's reasoning as to what constitutes a fraud upon the jurisdiction of the federal courts, the opinions distinctly make the statement that the principle of looking to the motives and intent of one who attempts to acquire citizenship for jurisdictional purposes, is not a new principle. The corporate entity, therefore, is here treated just as the courts treat a natural person. It is worthy of notice, also, that in each of the three cases discussed above, one from Virginia, one from Georgia, and one from California, the decision of the United States Supreme Court affirmed the decision of the lower court.

On the subject of agency the expression of the court in the Lehigh Mining and Manufacturing Company case is significant. In that case a Virginia corporation created a Pennsylvania corporation and conveyed property without consideration to it for the purpose of obtaining the jurisdiction of the federal

courts in a dispute that had arisen between the Virginia corporation and citizens of Virginia. The court said: "It is true that a technical title to the lands in controversy is, for the time, in the Pennsylvania corporation. It is also true that there was no formal agreement upon the part of that corporation 'as an artificial being, invisible, intangible, and existing only in contemplation of law' that the title should ever be reconveyed to the Virginia corporation. * * * But we cannot shut our eyes to the fact that there exists what should be deemed an equivalent to such an agreement, namely, the right and power of those who are stockholders of each corporation to compel the one holding the legal title to convey, without a valid consideration. * * * The stockholders of the Virginia corporation * * * assumed, as a body, the mask of a Pennsylvania corporation, for the purpose only of invoking the jurisdiction of the circuit court of the United States."[217]

In the Miller case the court also expressed itself on the point of agency. In that case, it will be remembered that all the property of the Nevada corporation was held as agent for a California corporation. Justice Harlan regarded the facts as indicative of the relation of principal and agent between the two corporations and held that therefore the fiction of separate corporate existence did not apply.[218]

I shall not undertake an extended consideration of the use by the courts of the doctrine of agency.[219] The principles employed are the same as those set forth by the United States Supreme Court in the cases above discussed.

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[217] This passage was also quoted in Miller and Lux, Inc., v. East Side Canal and Irrigation Co., 211 U. S. 294 (1908).

[218] See pp. 145ff, and pp. 149-150, *supra*.

[219] For discussion of this point by state courts see 49 Ohio St. 137, 177, 15 L. R. A. 145, 30 N. E. 279, 30 Am. St. Rep. 541; 30a Weekly Law Bul. 87 (Superior Court of Cincinnati); 93 N. W. 1024, 60 L. R. A. 927; 16 Lea, 27; 3 N. Y. Supp. 401, 2 L. R. A. 33; 155 Ill. 166, 39 N. E. 651, 27 L. R. A., N. S, 298; 59 Ohio St. 316, 52 N. E. 834; 42 N. Y. Supp. 781; 121 N. Y. 582, 621, 24 N. E. 834, 9 L. R. A. 33, 18 Am. St. Rep. 843; 142 Fed. 247.

There is a group of cases, however, which turn upon a question of attempted fraud quite different in kind from that before the court in matters of determining federal jurisdiction. Of these, there are two classes of cases of special importance to a clear understanding of the extent to which the courts will apply the doctrine of agency as a basis for disregarding the corporate entity to prevent fraud or injustice. These refer, on the one hand, to attempted fraud upon creditors, and on the other hand, to attempted circumvention of a federal statute.

The first class of cases is illustrated by the decision in Hunter v. Baker Motor Vehicle Company.[220] In that case the undeniable existence of a real separate entity appears. An Ohio corporation had formed a New York corporation to handle its goods. The Ohio corporation then formed a second New York corporation to take over the property of the first. The plaintiff recovered against the second New York corporation for a debt against the first. In its opinion the court said:

"The fact that stockholders of two corporations or the greater number thereof are the same persons does not operate to destroy the legal entity of either corporation. Nor does the fact that the one corporation exercises a controlling influence over the other, through the ownership of its stock, or through the activity of its stockholders, operate to make either the agent of the other, or to merge the two corporations into one." However, "there are at least two exceptions to the general rule of separate corporate existence and liability which are specifically applicable in this case, under the facts stated and admitted for the purposes of this demurrer: First, the legal fiction of distinct corporate existence in such cases will be disregarded, when necessary to circumvent fraud; second, it may also be disregarded in a case where a corporation is so organized and controlled, and its affairs are so conducted, as to make it merely an instrumentality or adjunct of another corporation."

[220] 190 Fed. 665, 668 (1911, C. C., N. D., New York).

This statement is especially interesting as it emphasizes a fact that must continually be borne in mind, namely, that it is not merely the identity of the individual stockholders of one corporation with those of another which offers an occasion for disregarding the separate existence of each corporate entity; nor is it the fact that one corporation controls the other by dominant stock ownership that gives occasion for the courts to disregard the separate entity of either body. But it is the person or persons in the relation of principal and agent which gives to the courts the ground, upon occasion, to recognize the identity of interests between the principal corporation and the agent, or *vice versa*. The separate entity of the agent corporation is not denied, any more than the separate existence of an individual principal or agent is denied. But where the charge of fraud causes the court to scrutinize all of the circumstances, the relationship of principal and agent, if it be found to exist, is recognized, even though the corporation is the agent of its own stockholders.

The statement of the law in the Baker Motor Vehicle Company case is in accord with the authorities generally.[221] The two exceptions are in most cases both involved together in the decision of a case that includes either.

A late case which deserves special attention is United States v. United Shoe Machinery Company.[222] The court therein indicated its disposition to regard one corporation that owned all the stock of another and controlled its policy and business, as responsible for the acts of a subsidiary corporation, which were considered in equity as its own acts. The case arose by a prosecution under the Sherman Anti-Trust Act against a combina-

[221] 2 Cook, Ed. 6, par. 663, 664, and p. 1983, and cases cited and discussed in note 3, p. 1984. Clark and Marshall, Private Corporations, par. 7 (e); 5 Thompson, Corporations, Ed. 2, par. 5470; Morawetz, Private Corporations, par. 227; 62 Ohio St. 189, 56 N. E. 1033; 78 Am. St. Rep. 707, 48 L. R. A. 732; 59 Ohio St. 316, 52 N. E. 834, and cases cited; 49 Ohio St. 640, 32 N. E. 167; 84 Md. 535, 36 Atl. 592; 67 Neb. 644, 93 N. W. 1024; 157 Fed. 600; 10 Mich. Law Rev.

[222] 234 Fed. 127 (D. C., E. D., Mo., June 6, 1916).

tion in restraint of trade. The officers and directors of three corporations were practically the same, and stock ownership and control were mutual. It was held that, "whatever may have been the views of the courts in earlier days, of corporate existence, when there were but few corporations, and they mostly confined to business of a quasi-public nature, at this date courts, and especially courts of equity, will look behind the corporate fiction, and if it clearly appears that one corporation is merely a creature of another, the latter holding the stock of the former, thereby controlling it as effectively as it does itself, it will be treated as the practical owner of the corporation when necessary for the purposes of doing justice."

A late case which illustrates the application of the doctrine of notice in establishing agency is that of Linn and Lane Timber Compnay v. United States.[223] A corporation was created and made a party to an effort to keep a title to land, which was wrongfully held by one Smith under the United States Patent Laws. An attempt by this means was made to conceal it until it was too late for the United States to take action because of the statute of limitations. A suit in equity was brought by the United States to annul the patents which had been issued under the Timber and Stone Act of June 3, 1878,[224] on the ground that the entries were fraudulent. Upon the facts as found by the two courts below the court stated: "We must take it that the corporation was a mere tool of Smith, and that its knowledge was his knowledge." The use by the court of the term "legal personality" assumes the existence of such an attribute in the corporate entity, although the language of the court does not disclose the basis of its reasoning, whether it be founded in fiction or reality. Mr. Justice Holmes merely said that, "It is open to some doubt whether the deeds were delivered until after they were recorded, and it seems open to none that recording the deeds was the first business the corporation did. This being so,

[223] 236 U. S. 574 (from C. C. of A., 9th Cir., Holmes, J.). See also McCaskill v. U. S., 216 U. S. 504.

[224] 20 Stat. 89; Timber and Stone Act of June 3, 1878, Chap. 151.

the difference in legal personality between Smith and the corporation gives the corporation no greater rights than Smith."

Thus the court did not hesitate to attribute to the corporation the capacity to be a party to the commission of fraud. "It cannot be privy to a fraud," said Justice Holmes, "and on the ground of its success set up a title of which another is to have substantially the whole advantage and thus defeat the adjudication that otherwise would undo the fraud. And it was held to be immaterial that before the bill was filed some of the shares of the corporation had been pledged for the defendant's debt. The court was of the opinion that this situation did not change the position of the parties as between the United States, Smith and the corporation in such a way as to give Smith a better standing in the case. Those who took the stock as security, it was pointed out, did not deal with the corporation as outsiders, but became a part of it while it still was under the manifest domination of Smith, and they were therefore charged with participation in his fraud. The corporation, therefore, could not derive any new right from them."[225]

It was thus held that, when a secret transfer of wrongfully held land is made in this way "for the purpose of busying the United States with the wrong person until the title shall be made good by time, service on the man thus put forward is sufficient to avoid the statute of limitations and the trick must fail."

Notice and Estoppel as Grounds for Looking Beyond the Separate Entity. Fraud may be prevented by the use of the doctrines of notice and estoppel to prevent a literal interpretation of the theory of separate corporate existence which would deny any relation between the wills of the individuals and that of the corporation. This is true even where there is no corporate agency averred. As I have pointed out in the discussion of the case of State v. Standard Oil Company,[226] the

[225] Citing 110 C. C. A. 232, 188 Fed. 545.
[226] 49 Ohio St. 137. See pp. 43ff, *supra*.

fiction that the separate corporate entity is in fact always distinct in its acts from the individual members who compose it cannot be accepted without limitation. Thus, the doctrine of notice was coupled with that of estoppel in Simmons Creek Coal Company v. Doran,[227] cited by the court in McCaskill Company v. United States.[228] It was there held that constructive notice to the members of a corporation was constructive notice to the corporation itself, where the facts showed that the corporate entity was merely being set up as a sort of non-conductor to relieve the Coal Company. When each and all of the individuals who organized a corporation under the state law had knowledge, or actual notice, of a defect in the title to lands acquired by the corporation through them, their knowledge or notice was knowledge or notice of the corporation, and if constructive notice bound them, it bound the corporation. However, it should be borne in mind that the case would be different where the constructive notice was notice not to "each and every" stockholder, but to one or a few only, who did not receive the same while acting as agents of the corporation. Every stockholder is not the agent of a corporation nor is an officer or director always such an agent whose knowledge or notice would be knowledge or notice to the corporation.

Another interesting situation in which the doctrines of notice and estoppel are used is that in which there is an attempted use of the corporate fiction fraudulently to defeat the effect of a restrictive contract. Thus, an individual who is bound to desist from manufacture or use of a certain article within a specified territory sets up a corporation and through the corporation attempts to evade his obligations. A strong federal case which deals with such a set of facts is that of National Recording Safe Company v. International Safe Company.[229] An individual, it is held, cannot be allowed to set up a corporation to evade a contract obligation which legally restricts him from doing

[227] 142 U. S. 417.
[228] 216 U. S. 515.
[229] Cir. Ct. N. D., Ill., E. D., Jan. 24, 1908.

certain acts individually. In this case knowledge of the three stockholders of an attempt, through incorporation, to evade the contract obligation was considered to be knowledge of the corporation when two of the stockholders derived their knowledge from the third, the dominant stockholder. The facts embraced the sale of a patent right by one Fisher, who received for it one-third of the capital stock of the complainant corporation, valued at $5,000, upon which he had been paid in dividends 42½ per cent., and had become a director of the company. Afterwards, and while retaining nominal connection with the complainant, he organized the defendant company, taking $12,000 of the stock out of a capital of $25,000 and assuming the position of secretary and treasurer. The defendant later began the manufacture of the alleged infringing portable safe. The facts, it was held, brought the defendant within the rule as to estoppel, which the court had laid down in Siemens-Halske Electric Company v. Duncan Electric Manufacturing Company.[230] For, it was said, the dominant stockholder was the moving spirit of the corporation and he induced the manufacture of the allegel infringing device. That he was estopped was granted, and the other two stockholders were held to be bound by the estoppel against him. The court, quoting from Mellor v. Carroll,[231] said: "If the estopped assignor enters into business, then others who derive from him their knowledge of the patent process or machine, and availing themselves of his knowledge or assistance, enter with him upon a manufacture infringing the patent which he has assigned, they are bound by his estoppel."

A very late case in Pennsylvania[232] holds that courts will prevent the use of the corporate form to escape a restrictive contract. It presented a situation in which, as distinct from the situation in the case just discussed, in which a new corporation was created, control over an existing corporation was acquired by individuals bound by a restrictive contract. A contract had

[230] 142 Fed. 157.
[231] 141 Fed. 992.
[232] 98 Atl. 956 (Pa. 1916). See Michigan Law Review, p. 264.

been made with certain persons and they later acquired all the stock and constituted four of the five directors of the corporation. Notice to these stockholders and officers was held to bind the corporation and to entitle the plaintiff to an equitable account.

The attainment of "equitable justice" where there is no fraud alleged has been held by the Supreme Court, in a very late case, to be a sufficient reason for looking beyond the separate corporate entity. Thus, the latest case in which the court seems to disregard the corporate entity involved a reorganized railway corporation and allowed a creditor of the old corporation to hold the reorganized body for the debts of the former, even where there was no fraudulent intent evidenced in the facts and circumstances surrounding the reorganization. In Southern Railway Company v. Guardian Trust Company,[233] the court held that if the reorganization scheme did in fact work out in an unforeseen way inequitably to the unsecured creditor, equitable relief would be granted by looking beyond the mere fact of separate corporate existence. Neither agency nor notice is here offered as a ground upon which to base the court's decision. Nor is the doctrine of estoppel expressly applied. Estoppel would seem to meet the facts, however, although its application would emphasize rather than disregard the separate corporate entity. Thus, the corporation seems to be estopped to deny the identity of its will with that of the previous corporation. But it is a strong case to show the tendency of the court to treat the corporation as a distinct and real entity without resort even to a fiction. It holds that the entity, though it sought to escape liability upon the ground of its strictly limited existence in law, yet in fact

[233] 240 U. S. 166, 60 L. Ed. 579, affirmnig and citing 201 Fed. 811, 210 Fed. 696, 228 U. S. 482. The 240th U. S. case affirmed the decision of the C. C. of A. of the 8th Circuit, from which an appeal had been taken to review a decree which, on a second appeal that reversed the decree of the District Court of the Western District of Missouri held that a certain unsecured creditor of a corporation could charge with its debt a new corporation formed under a reorganization scheme.

was treated as a distinct entity, but not exempt from liability in the particular case. The court did not deny corporate existence, but, recognizing the close association between the corporate will and that of the stockholders, and the identity of the stockholders in one corporation with those in its predecessor, dealt with the individuals to this extent: It refused to let a body of persons who had been indebted in one corporate capacity assume another corporate body and then set up that body as a nonconductor and deny the debt. Justice Holmes (the Chief Justice and Justice Van Devanter dissenting upon the ground that on the findings of the Master the decree should be reversed) said:

"The equities in favor of the trust company result from the consolidation alone, and from the express terms in the plan."

There is here no denial of the existence of a separate corporate entity. The Guardian Trust Company was a stockholder as well as an unsecured creditor of the Kansas City Suburban Belt Railroad Company which had had to undergo receivership and sale under foreclosure. The trust company exchanged its stock for that of the new purchasing corporation and it was said that by its retention of this benefit it had precluded itself from making a claim on the debt. The reorganization plan stated at the outset that one of the results to be attained was the payment of the floating debt and the existing car-trust obligations. It is true, said the court, that the provision which was made turned out to be too small. But "the plan did not on its face give notice of an intent to prefer Belt stockholders to its creditors, and therefore the trust company by assenting to it and exchanging stock under it lost no rights."

The appellant Railroad Company urged that the foreclosure sale was to be "treated as a distinct transaction and that after it had become the owner of the greater part of the bonds and stock of the Belt Company it was free to do as it pleased. If it had merely kept the stock it would have incurred no liability to creditors of the Belt Company, and the independent foreclosure would put it in no worse position."

The court, however, found in the intent and purpose of the purchasers at the foreclosure a reason for disregarding this argument. It looked to the whole transaction, and found that "ownership of the Belt Railroad by the new company was contemplated from the first, and although no fraud on creditors was suggested or intended in the plan, still the Court of Appeals was justified in regarding the whole proceeding."

Conclusion. From the discussion of cases in this and the preceding chapter we should be able to draw some conclusions. Certainly it may be said that today the Supreme Court of the United States does not deny the reality of the separate existence of the corporate entity. Its language, as well as that of the lower courts, does not guarantee us relief as yet from an inextricable maze of legal fictions. But the tendency is to apply the content of the fiction theory as to separate corporate existence of the entity, to the full extent of logical reasonableness in its complete significance, and then to forget the "fiction" and substitute reality. Realism may be expected to actuate the United States Supreme Court to grant citizenship to the corporate entity in fact as it in effect has done with its fictitious irrebuttable presumption. Realism will continue to look to the actual purpose of corporate organization and the intent of its incorporators, in order that it may discover whether, in fact, the object to be attained is within the scope of the avowed lawful purpose, lest it be tinged with fraud.

It cannot be too strongly emphasized that stockholders today are primarily investors and not proprietors.[284] The majority of the great industrial corporations have come to be, for the large number of small stockholders whose cumulative savings make the great industrial and commercial corporate undertakings possible, a mere safe depository for earnings which bear interest,

[284] Dewing, Industrial Promotions and Reorganizations (1913); W. I. Lyon, Capitalization (1916); C. W. Gerstenburg, Materials of Corporation Finance; E. S. Meade, Corporation Finance.

or the possibility of interest, on a supposedly safe investment. While theoretically the stock represents a share in "proprietorship" or "ownership" in the corporation, as a matter of fact, most small investors have neither the time nor the ability to follow or understand the financial and industrial operations of the large corporation. Hence the relation of trust that is said to exist between directors and stockholders. Wherefore the corporation as a separate entity, together with its directors and officers who control its policy and direct its affairs, are to an increasing extent being required to submit to the scrutiny of courts of equity. Their actions are measured by the fiduciary relation that is said to exist despite the customary blanket clause usually put through at the annual stockholders' meeting technically and legally endorsing and ratifying all acts of the board of direcotrs and officers for the year past. The attitude of the courts is strikingly set forth by the Supreme Court of the United States in McCaskill v. United States.[235] Justice McKenna said:

"Undoubtedly, a corporation is, in law, a person or entity entirely distinct from its stockholders and officers. It may have interests distinct from theirs. Their interests, it may be conceived, may be adverse to its interests, and hence has arisen as against the presumption that their knowledge is its knowledge, the counter presumption that in transactions with it, when their interest is adverse, their knowledge will not be attributed to it. But while this presumption could be enforced to protect the corporation, it should not be carried so far as to enable the corporation to become a means of fraud or a means to evade its responsibilities. A growing tendency is therefore exhibited in courts to look beyond the corporate form to the purpose of it and to the officers who are identified with that purpose."[236]

[235] 216 U. S. 504, 514, cited in 234 Fed. 127.

[236] Illustrations of this principle, said the court, are given in Cook's Treatise on Corporations, par. 663, 664, 727. It was enforced in Simmons Creek Coal Co. v. Doran, 142 U. S. 417.

PART II.

THE CORPORATE ENTITY IN MARYLAND LAW.

CHAPTER VI.

HISTORICAL BACKGROUND.

The purpose of the discussion of Maryland cases in this chapter is to point out the peculiarities of the Maryland law as they appear in the decisions of the Court of Appeals, and to note whatever divergence there may be between the theory and practice of Maryland as compared with the law as it is interpreted elsewhere. To explain such conclusions as may be established on this basis, it is essential to examine the theories underlying corporate existence when they have appeared in this state, and the concepts adopted by the court in arriving at its interpretation of the law. The attitude of the court on questions arising out of the treatment of *ultra vires* acts of a corporate body or its officers will necessarily be determined by the conception of the relation of the corporation to the state entertained by the court, and this, in turn, goes back to its theory of corporate existence and the nature of the corporation.

The same is true as to the degree of liberty of action accorded a foreign corporation doing business within the limits of the state. And the whole field of problems surrounding the birth, continuing existence, and forfeiture or death of the corporate body, hinges upon a preliminary decision as to what shall be the explanation and legal definition of a group of individuals so organized.

For these purposes, it is not necessary to enter into a detailed classification of corporations on the basis of pronouncements of

the Maryland court. They are, in their nature, similar to such bodies everywhere. Classifications in Maryland law do not differ from those already suggested in Chapter II.

Nor is it necessary, in order to arrive at conclusions sought in this chapter, to go into the history of the corporate form of organization in Maryland. Suffice it to say, that in Maryland in colonial times there were no private corporations.[237] It is as true of Maryland, therefore, as of other states that the doctrines of corporate existence found in the decisions of the Court of Appeals had their origin in a period when the modern form of ordinary private business corporation was unknown. Hence, the unsuitable philosophy of the nature of the corporation and the restiveness with which those who seek the benefits of incorporation chafe at the inelasticity of the corporate form of organization.

"All lawyers will agree," says Mr. Arthur W. Machen, Jr., addressing the Maryland Bar Association in 1909,[238] "that there is often great difficulty under even the most liberal corporation laws, in doing what you want to do." "That the law ought not wantonly to thwart or obstruct commercial or industrial enterprise," he says, "may be accepted as an axiom of jurisprudence."[239] And, "Almost equally axiomatic—at least in this day and generation—is the proposition that as a general rule and subject to but rare exceptions, the most efficient means of starting and carrying on any business that requires a considerable capital is through the instrumentality of an incorporated company." Yet this proposition, he says, "even if it be self-evident, has not been demonstrated by experience," and, "unless the law is to place obstacles in the way of the prosecution of business enterprise * * * it must permit the promoters of any legitimate undertaking to prosecute it in the most effective

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[237] McKim v. Odom, 3 Bland, 407.

[238] Machen, Do the Incorporation Laws Allow Sufficient Freedom to Commercial Enterprise?—Report of the Fourteenth Annual Meeting of the Maryland State Bar Association (1918), p. 78.

[239] Ibid., p. 81.

manner, or in other words to form a corporation with such powers and subject to such regulations as they may deem best adapted to their own circumstances."[240]

Of course, Mr. Machen does not mean by this that every feature of corporate organization must be left to the determination of the promoters, but "the burden of proof is upon those who assert that there should be any particular legislative restraint." "Liberty," he says, "is the normal state of the American citizen; if you are to restrict his freedom, the burden is upon you to establish the wisdom and necessity of the restriction."

Having thus stated the problem to be met by what he conceives to be a proper legislative attitude towards corporations, Mr. Machen proceeds to explain the difficulties in the way of attaining it. First among them he suggests the historic misapplication of theories of the nature and the existence of the corporation which grew up in the monopolistic period of corporate enterprise prior to the nineteenth century. "With respect to incorporation," he says, "the truth of this principle (that is, of freedom) is obscured by a number of circumstances. First among them is our legal history. Inasmuch as no corporation could be formed at common law without a special franchise, we reason that the right to incorporate is in its very nature a special privilege to be granted only on narrowly defined conditions. It would be as logical to argue that the right to devise real estate is a franchise to be granted only on narrowly defined conditions, because forsooth the right did not exist prior to the Statute of Wills; or that the right of a person accused of crime to enjoy counsel for his defense is a franchise to be jealously guarded and limited because that privilege was not allowed at common law. The truth is that in all these cases, the *common law was wrong.* The effect of a modern general incorporation law is to abrogate this inconvenient and unfortunate rule of the common law which prevented citizens from incorporating

[240] Ibid., p. 82.

by their mutual agreement. That rule of the common law is now as obsolete as the law of fines and common recoveries."

With suggestive effect Mr. Machen points out the baleful influence of our historical past. "Yet how often," he continues, "among lawyers as well as among laymen, the notion survives that a corporation is a creature of the state graciously presented by a dread sovereign with the right to exist, and that therefore it ill becomes the creature to complain of any limitations, whether reasonable or unreasonable, that its creator, the State, may impose. Shall the clay complain of the potter? Shall the thing formed say to him that formed it, 'Why hast thou made me thus?' We can never grasp the fundamental theory of general incorporation laws until we appreciate that corporations formed under such laws—even the most illiberal of them—are the creatures not of the State, but of the corporators. All that the State does is to abrogate *pro tanto* the rule of the common law which required a charter of the crown as a prerequisite to the formation of a corporation. The State removes the obstacle interposed by the common law to the formation of a corporation; but it is the incorporators who create the corporation. The corporators are the parents of the company; the function of the State is merely that of the officiating clergyman at the wedding—to bestow its blessing on the union of natural persons which is to result in a new personality."[241]

The baneful influence of that part of Chief Justice's Marshall's decision in the Dartmouth College case which projected the mediæval English fiction theory of corporate existence into our law, is recognized by Mr. Machen as another obstacle which has stood in the way of legislation as well as of judicial progress toward the emancipation from the outgrown theories which have fettered private corporate enterprise. Inasmuch as I have referred to that case and the similar doctrines of Chief Justice Marshall in the Deveaux case and the Bank of Augusta v. Earle, I will venture again to quote Mr. Machen in full on the sub-

[241] Machen, Op. Cit., pp. 83-84.

ject. His testimony distinctly bears out the conclusions that have been reached in Chapter III. "The Dartmouth College case," he points out, "is another factor that has tended to obscure the right of the people to freedom from vexatious legislative interference and restrictions in the formation and management of corporations. That decision not unnaturally aroused an almost insane jealousy of corporations as chartered monsters to be allowed only such liberty as they could in each individual case affirmatively prove would not be abused. This attitude persisted, and in many quarters still persists."

Another historic point that it is pertinent to a discussion in this chapter to bear in mind is the fact that, prior to the passage of the Corporation Act of 1908,[242] the laws of the State of Maryland pertaining directly to, or materially affecting, corporations, represented an unorganized state of confusion.[243] During the nineteenth century the Maryland legislature was quite as conservative as the Court of Appeals itself, and no definite legislative or judicial classification or clarification of the laws relating to corporate organization and existence was attempted. Mr. Machen's address before the Maryland Bar Association, from which I have quoted, was delivered one year after the passage of this Corporation Act, and he took note of the vast improvement in the law in the following words: "For us in Maryland who are now for the first time enjoying the

[242] Laws of Maryland, 1908, Chapter 240.

[243] George M. Brady, Maryland Corporation Law (1914), Introduction, p. xxxix. Mr. Brady speaks of the corporation laws of the period prior to 1908 as constituting a "maze of planless legislation." And in his Preface, at page xxxvii, he says: "Prior to the passage of Chapter 240 of the Acts of 1908 the laws of Maryland relating to corporations constituted a hotchpotch of acts, amendments, repeals and re-enactments frequently passed without the slightest regard to prior Acts or existing statutes. The Act of 1908 was intended to be the embodiment of the local and fundamental principles regulating modern business corporations. It was the first and most important of the several recent legislative enactments relating to corporations. Since then numerous other and important changes in the law have been made." The principle changes are embodied in the Acts of 1914, 1916, and 1918.

benefits of a statute which is not, to use the words of a well-known writer, a mere 'legal antique' or curio, it is especially fitting to consider the true theory of modern incorporation laws, * * * in order that inharmonious and injudicious amendments to our new law may be averted."[244]

It is not necessary here to discuss the provisions of the Maryland Acts. It is sufficient to note that, while of very great practical benefit, the larger part of their provisions do not rest upon any fundamental change in the attitude of the legislature as to the theories of the nature of the corporation. For instance, the purposes for which corporations might be formed under the general laws were broadened by the Act of 1908, and the requirements as to the number of incorporators was reduced from five to three, and only one, instead of a majority, was required to be a citizen of the state. The minimum number of directors was reduced from four to three, and the maximum of twelve was no longer specified; and only one, instead of a majority of them, was required to be a citizen of the state. An executive committee which might be elected from the members of the directorate, under the new law, does not have to include any citizens of the state. No certificate of incorporation may, under the new law, be declared void for formal defects merely; and where an effort is made in good faith to form a corporation, its legality cannot be questioned.

An important change as to foreign corporations under the new law of 1908 provides that only those classes of corporations now permitted to be formed in Maryland can transact their business within the state. On the matter of the internal organization of the corporation, the power to make, alter and repeal by-laws was given to the members and shareholders, and not to the directors, and careful provisions are substituted for the obscure and unsatisfactory statement of the old law as to the calling of regular, general, and extraordinary meetings. Stipulations are made whereby any corporation may provide through cumulative voting for representation in the election of directors.

[244] Machen, Op. Cit., p. 80.

The procedure by which two or more corporations organized under the laws of Maryland may be consolidated to form a new corporation is set forth. The right to demand statements and inspect books of the corporation is confined to "any person or persons holding in the aggregate five per cent thereof, if two or more classes (of stock) have been issued." The usual provision is made as to the limited liability of stockholders, and no stockholder, except in the case of banking corporations and those classes of corporations for which special provision is made, is made liable to creditors for the corporate debts. As is usual, the stockholder's only liability is to the corporation or its receiver for any unpaid part of his subscription. Every corporation is guaranteed the right of perpetual succession, and all provisions in the charters or certificates of incorporation existing at the time the new law went into effect limiting their existence were repealed. Provision was made for voting trusts for a period not exceeding five years, and for reorganization when property and franchises are sold under judicial proceedings.[245]

This summary of the principal changes in the corporation law of Maryland in 1908, although indicative of no fundamental changes in the theory of the nature of the corporation, shows that it was deemed advisable to make the corporate form of business organization more practically useful; and to that extent the new laws denote a more liberal attitude on the part of the legislature. That such an attitude is extremely wise, must be inferred by the very marked increase in the annual formation of corporations during the last ten years since the laws went into effect. Tables III and IV, with the accompanying diagrams, indicate the increase in the number of private corporations formed each year and the impetus given this commercial and industrial tendency to use the corporate form of doing business by the new incorporation laws. The number

[245] Proceedings of the Maryland State Bar Association, 1908; Report of the Committee on Laws, p. 37.—Important Changes Made in Existing Law, p. 48.

TABLE III - NEW CORPORATIONS FORMED IN MARYLAND UNDER GENERAL INCORPORATION LAWS

The period covered in this table begins in 1891 when the filing of a certificate of incorporation with the State Tax Commissioner and the payment of a bonus tax were first required as conditions precedent to legal corporate existence. New corporations formed during an annual period are listed for alternate years. From 1899 amendments to charters are tabulated separately. The total number filed, therefore, is the sum of the two figures.

Source of information: Reports of the Maryland Tax Commissioner, 1891-1914; Reports of the State Tax Commission, 1915-1917.

Fiscal[a] year	New corporations	Amendments	Fiscal[a] year	New corporations	Amendments
1891	85	—	1905	325	23
1893	331	—	1907	351	56
1895	148	—	1909	688	60
1897	122	—	1911	716	101
1899	185	2	1913	740	132
1901	252	12	1915[b]	963	161
1903	409	17	1917[c]	960	184

a - Year ends September 30
b - June 1, 1914 to December 1, 1915
c - June 1, 1916 to December 1, 1917

NEW CORPORATIONS AND AMENDMENTS LISTED FOR ALTERNATE YEARS

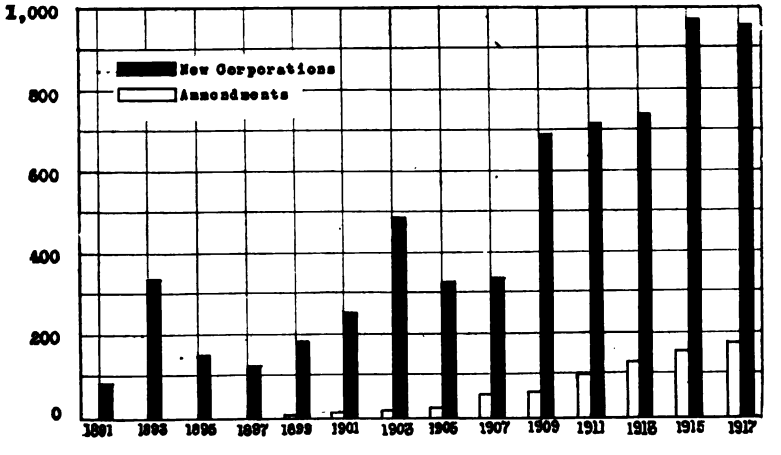
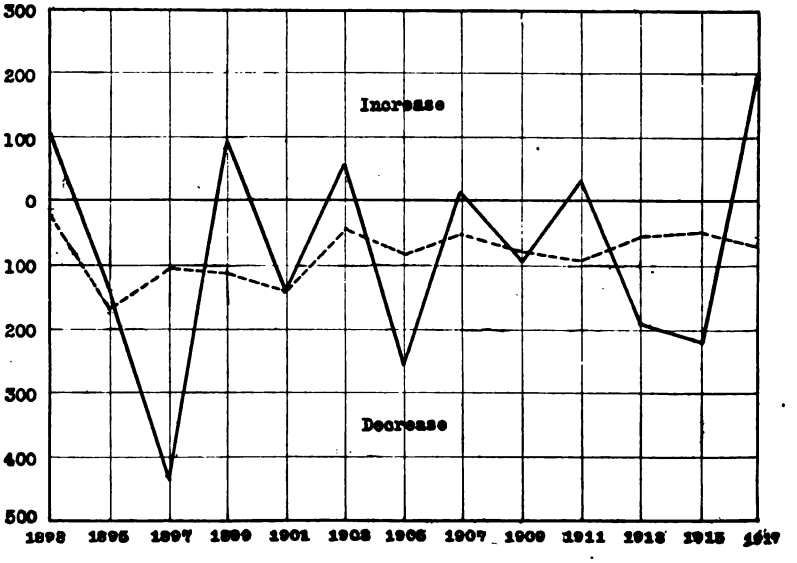


TABLE IV - NET INCREASE OR DECREASE IN CORPORATIONS IN MARYLAND

There are no records available as to the number of inactive corporations which have been dissolved by a court proceeding. The number of "deaths" therefore, can only be approximated. The following curves are based upon the difference between the number of corporations assessed for taxation in a given year and the number listed as assessed in the preceding report plus the new corporations formed in that year.

The broken curve shows the same figures plotted as a moving average and indicates a general trend of mortality as between 23 and 157 yearly.

Source of information: Reports of the Maryland Tax Commissioner, 1891-1914; Reports of the State Tax Commission, 1915-1917.



of new corporations formed in 1909, one year after the first revision of the corporation laws, showed an increase of thirty-two per cent over the number formed in 1907, one year preceding the new law. And in 1917, a decade after the new law went into effect, the annual number formed was nearly four hundred per cent of the number formed in 1899, a decade before the law became effective, and nearly ten times as great as the records of the State Comptroller indicate as having been formed in 1891.

Table V points out the striking increase during the past thirty years, in the number of cases before the Maryland Court of Appeals which have involved private corporations. Over fifty per cent of the litigation in the highest state tribunal has to do with the affairs of private corporations. Not all of these cases involve the corporation as a party to the suit. Nor does every case arise directly out of a variance in interpretation of the nature of the corporate entity. But the figures and diagrams of this table, together with those in Table VI, indicate the tremendous importance of the ordinary business corporation in the economic and political life of modern society, and the undoubted benefits that must accrue from a more positive attainment, by the judicial tribunals of the states, of settled and uniform theories of corporate existence and of the nature of the corporate entity. The status of the fiction theory must be more clearly and universally defined than it is today. Possibly this duty will ultimately fall upon the legislatures, as it has fallen to the Maryland Legislature to initiate positive reforms in the corporation laws. But the philosophical interpretation of the nature of the corporation upon which the great mass of the rights of the entity, and, therefore, those of the individuals also, rest, must always be supplied by the judicial tribunal which interprets legislative provisions.

I do not mean to infer that the percentage of total litigation arising from questions of corporate activity, which occupies the attention of the courts today, will necessarily show an absolute

TABLE V - MARYLAND LITIGATION INVOLVING PRIVATE CORPORATIONS

The increase in the percentage of cases before the Maryland Court of Appeals, which involve private corporations is evidence of the growth in numbers of corporate bodies of that type.

Private corporations did not exist in Maryland in the Colonial period. The first third of the nineteenth century saw a rapid development of these institutions. The first general incorporation law was passed in 1808. Its principal revisions occurred in 1908, 1914, 1916 and 1918.

Source of information: Reported decisions of the Maryland Chancellors and Court of Appeals, Law Library of the Supreme Court of the United States; Reports of the Comptroller and the Tax Commissioner of Maryland, 1878-1914, and of the State Tax Commission, 1915-1917.

Volume of report	Date of decision	Total cases reported	Cases involving private corporations	Cases involving private corporations in per cent of total
3 H.&M'H.	1790-1797	129	0	0
7 H.& J.	1825-1826	54	10	18
9 Gill	1850-1851	67	4	6
16 Md.	1860	47	10	21
33	1870	73	14	19
54	1880	65	15	23
72	1890	69	26	37
91	1900	62	31	50
112	1910	61	32	52
131	1917	87	43	50

reduction, but the cases which spring from disagreement over the acts of the corporate entity and the members, due to the unsettled or non-uniform interpretation of the so-called Anglo-American fiction theories of corporate existence, will certainly decrease. There will be gained the undoubted advantage of a settled condition of the law, whatever it may be. For instance, it is undoubtedly true that the state of judicial interpretation of the law appertaining to the payment of the bonus tax, and other formalities regarded as essential prerequisites, conditions precedent, to the beginning of corporate existence or the exercise of corporate powers, has not undergone a change during the period subsequent to the revision of the corporation laws of 1908 by the legislature. The interpretation of that law has been in a settled state during this time, as has also the Maryland law bearing upon *ultra vires* acts of a corporation. Yet, as graphically indicated in Table V, the per cent. of litigated cases involving private corporations has not decreased. A possible and very reasonable explanation may be deduced from the large increase in the number of corporations formed annually, as indicated in Table III. There may well have been a decrease in the class of cases which have grown out of uncertainty of the judicial interpretation of corporate theories and concepts, and at the same time the great increase in the number of corporations formed during this period must necessarily have brought before the court questions of ordinary rights and obligations whose determination did not rest upon principles different from those which determine similar rights and duties of individuals.

Tables VII and VIII bear out the suggestions of Tables III, IV, and V, as to the prominence of corporations in the modern social, economic, and political organization of the state, and they call attention to the increase in relative numbers of corporations of various types as compared with the whole number of corporations assessed in a particular year and at the beginning and end of a given period. It is of interest to note that the aggregate amount of state taxes assessed upon all corpora-

TABLE VI - MARYLAND COURT CASES INVOLVING CORPORATIONS OF ALL TYPES

The increasing number and prominence of ordinary business corporations in the past fifty years is indicated by the rapid growth in the amount of litigation involving them before the Court of Appeals during that period.

The term, ordinary business corporation, is here used to include all private corporations other than banking or trust, and insurance companies. The term, public corporation, as here used, does not include the State. The larger part of this class is made up of municipal corporations.

The relatively few cases involving two types of corporations have been listed only under the heading of private or public corporations, the former class taking precedence.

Source of information: Reported decisions of the Maryland Chancellors and Court of Appeals, Law Library of the Supreme Court of the United States; Reports of the Comptroller and the Tax Commissioner of Maryland, 1878-1914, and of the State Tax Commission, 1915-1917.

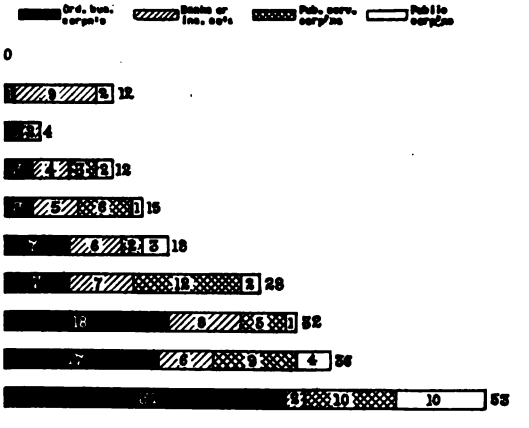
Volume of report	Date of decision	Total cases reported	Cases involving corporations				
			Private			Public	Total
			Ordinary business	Banking or insurance co's	Public service		
3 H.& McH.	1790-1797	129	0	0	0	0	0
7 H.& J.	1825-1826	54	1	9	0	2	12
9 Gill	1850-1851	67	2	2	0	0	4
16 Md.	1860	47	3	4	3	2	12
33	1870	73	3	5	6	1	15
54	1880	65	7	6	2	3	18
72	1890	69	7	7	12	2	28
91	1900	62	18	8	5	1	32
112	1910	61	17	6	9	4	36
131	1917	87	31	2	10	10	53

TABLE VI (GRAPHICALLY PRESENTED) - MARYLAND COURT CASES INVOLVING CORPORATIONS OF ALL TYPES

The rapid development in the use of the ordinary business corporation in the past thirty years is suggested by the marked increase in number of litigated before the Maryland Court of Appeals, in which this type of corporation has been involved.

A comparison of this diagram with Tables I and II indicates that public service corporations were much less prominent in litigation before the Maryland tribunal than they have been in the Supreme Court of the United States.

Volume of report	Date of decision	Total cases reported
3 H.&McH.	1790-1797	129
7 H. & J.	1825-1826	54
9 Gill	1850-1851	67
16 Md.	1860	47
33	1870	73
54	1880	65
72	1890	69
91	1900	62
112	1910	61
131	1917	87



tions in 1879 amounted to $100,292.00, while the amount assessed in 1917 in incorporated towns against ordinary business corporations alone was over $7,828,000.00, and that against the real estate and rolling stock of steam railroads was $53,699,000.00. Diagram VIII bears out the conclusions suggested by the diagram accompanying Table VI. It emphasizes the marked increase in the number of ordinary business corporations formed under the general laws, as compared with special types of private corporations.

A comparison of all of these tables suggests that there is a positive relation between the economic condition of the country and the organization and dissolution of corporations as pictured for alternate years in Tables III and IV. There are no records available as to the number of inactive corporations which have not been dissolved by court proceedings; hence the basis of estimate assumed in Table IV. After twenty years of urgent recommendation by the State Tax Commissioners, an act was passed in 1918 which requires the Comptroller annually to report to the Governor the corporations which are in arrears in the payment of certain taxes, and, after service and publication, to initiate court proceedings to dissolve those that do not respond. An unofficial estimate of the Comptroller in March, 1919, placed the probable number of dissolutions that will occur under this law in 1919 at about one thousand. This, however, would represent the cumulative total of corporations which have ceased to be active or never have been active during the preceding years, but have not undergone judicial dissolution.

The total number of litigated cases before the courts also reflects in varying degree the financial status of the country.

This brief statement of historical facts as to the position of corporations in Maryland suffices to point out the importance of attempting to understand the theories of corporate life and the nature of the corporation, upon which rests the conception of the corporate entity in Maryland law. Further historical facts as to the development of the various types of corporate organi-

TABLE VII - INCREASE IN CORPORATIONS ASSESSED ANNUALLY IN MARYLAND

The table and diagram show corporations assessed by the first State Tax Commissioner and the last to hold office before the creation of the State Tax Commission. The total increase is in part due to improved methods of assessment and revised taxation laws, but may be largely attributed to the great increase in corporations formed. Miscellaneous here includes public service, and private corporations except those otherwise classified.

Source of information: Reports of the Tax Commissioner, 1879 and 1914.

	1879	1913
Insurance Companies	15	11
Banks, Trust Companies and Sav'gs Inst'ns	58	238
Miscellaneous Corporations	440	4,812
Total	513	5,061

COMPARISON OF CORPORATIONS ASSESSED

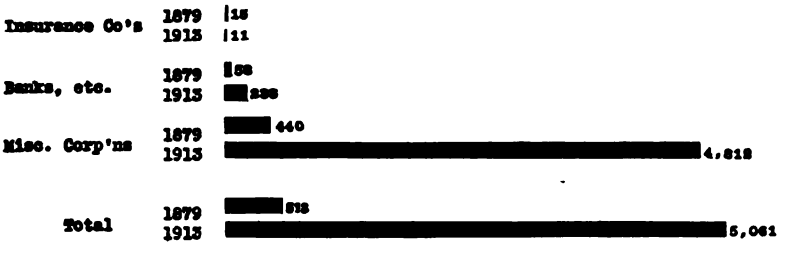


TABLE VIII - CLASSES OF CORPORATIONS SUBJECT TO ASSESSMENT BY THE STATE TAX COMMISSION OF MARYLAND

The table represents each class of corporations assessed. The classifications do not necessarily signify a legal difference in the nature of the corporate body, but represent groups defined by law and the usage of the Tax Commission for purposes of taxation.

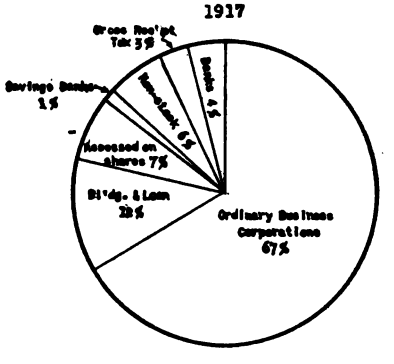
Ordinary business corporations here include all corporations having a capital stock except banks, trust companies and other financial institutions, and a large class of public service corporations. Corporations subject to assessment on shares include trust companies and financial institutions other than banks subject to the one per cent local rate, and public service corporations. Some of the latter type are also included in the class subject to the tax on gross receipts.

The diagram shows in per cent of total number the relative size of each class.

Source of information: Reports of the Maryland State Tax Commission, 1915, 1917; Laws of Maryland, 1914, chap. 324, sec. 88-B.

Class	1915	1916	1917
Ordinary Business Corporations	2757	3327	3479
Building and Loan Associations	580	622	643
Corporations assessed on shares	339	347	368
Banks	181	187	188
Savings Banks	45	34	47
Non-stock Companies	25	289	312
Corporations taxed on gross receipts	136	164	186

CLASSES OF CORPORATIONS IN PER CENT OF TOTAL



zations will appear in the following discussion of significant cases in Maryland, as will their classification:

The Corporation as a Person in Maryland Law. It is well settled in Maryland law today that the word "person," when used in a statute, "shall include corporation, unless such a construction would be unreasonable."[246] This has been the condition of the law since 1888. Yet prior to that time, before the legislature settled the matter, conflicting decisions of the Maryland Court of Appeals resulted in confusion. And since that date there are well-defined exceptions, in which it has been held "unreasonable" to include corporation within the meaning of the term "person." It was difficult to know just what was the status of the law in this respect. Indeed, Judge Miller expressly stated that the Maryland rules of interpretation were different from those of most of the other states.[247] It is of interest, therefore, to review the expressions of the Maryland court on this subject and to observe what bearing they have upon the concepts of the court as to the nature of the corporation. It should be understood, however, that the use of the term "person" in a statute does not of itself necessarily hold any special significance as to the nature of the corporate entity. It may be simply a general use of a word such as the use by which the pronoun "he" is used as inclusive of both genders. Yet the pronouncements of the court in interpreting the term may be more significant than the statute itself. Consequently, they are here set out at some length.

The terms "inhabitant" and "surety," as used in Maryland legislation, have come before the court for interpretation as to whether or not they include corporations. In its decision that they do include such bodies, the Maryland court was in accord with the findings of the Supreme Court of the United States and the tribunals of other states. In the early case of The Sable

[246] Laws of 1888, chap. 36, sec. 12, Code of 1904, Art. 1, sec. 14.
[247] 63 Md. 571 (1885).

Company[248] this question was before the court. The decision reflects the strict doctrine of the theory of existence of foreign corporations.

An action was brought against an association incorporated under an Act of 1819. The question as to the legal residence, domicile, or habitation of a domestic corporation within a county of the state came up for decision. In the course of the opinion, it was said: "As to what may be deemed residence of a corporation, it may be well to observe that as no government can give to its laws any extraterritorial operation, all bodies politic must necessarily be considered as social beings of that country by whose government they were incorporated and alien entities in all other countries; that a corporation may in the country of its origin have a fixed legality and residence from its nature and the terms of its creation; * * * and that all corporations, such as banks, etc., which are transitory in their nature and which are alien by the terms and nature of their creation and objects, may be considered as domiciled for some purposes, in that county of the state by the government of which they have been created, where they transact their business, or that county in which their property is."

And the court went on to point out that, "It is said that the name of a body politic is sometimes taken from the place of residence, because a corporation has a fixed place where it is settled and since it cannot be removed like a natural person, therefore, that a *distingas* against it to compel obedience to an order or decree must be directed to the sheriff of the county where it has a residence."

The question as to the meaning of the term "surety" came before the court in Gans v. Carter and Aiken.[249] Judge Briscoe held that that section of the state constitution which declares that "the General Assembly shall pass no law for any case for which provision has been made by existing general law," did

[248] 3 Bland, 606 (1823).
[249] 77 Md. 9 (1893).

not render unconstitutional the charter of the Fidelity and Deposit Company of Maryland, because it granted that corporation power to act as sole surety in all cases, where by existing general law no less than two were required on the bond of a trustee for the benefit of creditors. "Corporations," said the court, "were not included in the provisions of the general law relating to sureties on a trustee's bond set forth in section 205 of article 16 of the Code of 1888. That section still remains in force, but it applies to the suretyship of natural persons."

The question of whether or not the term "person" in a statute includes corporations came before the Maryland Court of Appeals in 1854 in the case of Germania v. State.[250] In that case the interpretation of the Act of 1824[251] was the point at issue. That act provided that "any person keeping or exhibiting for use a billiard table or tables without first obtaining a license shall forfeit the sum of $500." The Act of 1826[252] authorized the granting of a license to such person or persons as may apply for permission to keep a billiard table, and for such license there shall be paid the sum of $100. The third section of this act was substantially the same as that of the Act of 1824. The court held the corporation liable. Its decision was based on the statement of the law in Louisville Railway v. Leston.[253] The court said: "In view of the law a corporation is to be regarded as a person." "The appellant, therefore, is covered by the *descriptio personnæ*" of both the acts of assembly.

In 1885 the question again came before the court in the Crowther case.[254] This time the question was raised upon the interpretation of article 75 of section 87 of the Code of 1860, which provided that "no person should be sued out of the county in which he resides until after the return by the sheriff of the

[250] 7 Md. 6.
[251] Laws of 1824, chap. 64, sec. 3.
[252] Laws of 1828, chap. 129.
[253] 2 How. 508.
[254] 63 Md. 571 (1885).

county in which he resides of *non est* on a summons issued in said county."

In that case one of the questions was whether a turnpike company whose office was in Baltimore City could be sued in Baltimore County, and it was held that a corporation was not within the terms of the act above quoted. Judge Miller said in his opinion: "The rules of interpretation laid down in our code do not, as they do in most of the states, provide that the word 'person' shall be considered as including corporations." This was an unequivocal statement of the law by the Court of Appeals, as it existed prior to the Act of 1888,[255] and seems to have been in direct conflict with the case of State v. Germania decided twenty-one years before. In Crowther's case, however, the court held that the turnpike company whose principal office was in Baltimore City could be sued in Baltimore County, because "it was as much engaged in prosecuting the work for which it was brought into being" in Baltimore County, through which its road extended, as in Baltimore City, where its principal office was located. In this the court followed the common law rule that the residence of the corporation is the place where its principal office is located or where its principal operations are carried on.

In 1899 the court was again called upon to determine whether or not the word "person" was meant by the legislature to include corporations. In Henderson v. Maryland Home Fire Insurance Company,[256] Judge Pearce, relying on the rule of interpretation laid down by the legislature in 1888, decided that it did. The facts in that case show an attempt to sue a fire insurance company in a county other than that in which its principal office was located and its principal business was carried on. A plea to the jurisdiction was set up, based upon the common law rule that the place of residence of a corporation is the place where its principal office is located, or the location

[255] Code 1888, art. 1, sec. 12.
[256] 90 Md. 48.

of its principal business operations. The plea was based on the assumption, as the court said, that "there is no statute in Maryland which can be held to affect the application of that rule to this case." But the court was of the opinion that the common law rule had been abrogated in Maryland, and that, therefore, it was not required to consider the argument of the appellant, that the Act of 1896 authorizing the change of the appellee's office from Crisfield to Baltimore, was unconstitutional and void.

Since Crowther's case, the Act of 1888[257] had been passed, which provided that the word "person" "shall include corporation unless such construction would be unreasonable," and it was held by Judge Pearce in the Maryland Home Fire Insurance Company case to apply to corporations as well as to natural persons. The court called attention to the fact that the same legislature which had passed this act also passed the act which provided that "any person who resides in one county and carries on any regular business or habitually engages in any avocation or employment in another county may be sued in either county."[258] In reversing the interpretation of section 132 of article 75 as it had appeared in article 75, section 87 of the Code of 1860, Judge Pearce discussed these conflicting interpretations of the word "person." He said: "If the view of the law expressed in 63 Maryland[259] was then the correct view, the law has been changed by article 1, section 12, and if the view expressed in 7 Maryland[260] was then correct, the rule enacted in article 1, section 12, instead of changing the rule, was designed to declare it, and also to restrict its application where such construction would be unreasonable. When the character and extent of the business of successful fire insurance companies is considered we cannot imagine any ground upon which the court could hold such construction unreasonable." If this view of the law be adopted, said Judge Pearce, corporations

[257] Laws of 1888, chap. 36, sec. 12.
[258] Code of 1888, article 75, sec. 132, Laws of 1888, chap. 456.
[259] Crowther's case.
[260] Germania v. State.

are within section 132, article 75, unless such construction would be unreasonable in a given case or unless they are created under the general incorporation law. In the latter case they come within section 296, article 23, sub-head "Corporations." By that section all suits against such corporations are required to be brought where their certificate is properly recorded.

The status of the Maryland decisions as to the nature of the foreign corporation seems to be in accord with the so-called "strict" interpretation of the theory of the nature of the corporate entity. It is suggested that the statement of the law made by Judge Miller in Crowther's case may have been influenced by this narrow application of the fiction theory of corporate existence which the court felt called on to apply during the same year when dealing with a foreign corporation. For instance, in the case of Smith v. Silver Valley Mining Company[261] it was held that a foreign corporation could have no existence outside the state of its creation. In that case a corporation authorized by an act of the North Carolina legislature which had met and attempted to organize in Maryland, and which had held all of its meetings and conducted all of its business in Maryland and never accepted the charter in the state under whose authority it presumed to act, could not be given any recognition by Maryland courts as a legally existing entity.

In this case the Court of Appeals set forth at length what it conceived to be the Maryland law at that time as to foreign corporations. "The doctrine that a corporation must exist in the place of its creation," said the court, "and cannot migrate to another sovereignty, is so reasonable and just, and so firmly imbedded in our jurisprudence, that courts ought to have no hesitation in enforcing it." "But," said Judge Miller, "it would be of little practical utility, if corporators under an act passed by one state can leave it and go to another and there accept the charter, effect an organization, and thus bring the corporation into existence in a different sovereignty, and there proceed to

[261] 64 Md. 85.

act under it until restrained by a writ of *quo warranto.*" "Such acts," thought the court, "are mere usurpations of power and mere attempts to exercise authority by persons destitute of it, and should, in our judgment, be declared inoperative and void, no matter what the consequences may be, whenever they are, as they have been in this case, clearly proved, and a court is asked to grant relief to a suitor whose right thereto is founded upon their assumed or supposed validity. There is no rule of comity such as requires one state to be made the birthplace of a corporation chartered in another."

It was held that directors of a corporation might hold meetings, have an office, make contracts and transact part, at least, of the general business of the corporation within another state, unless prohibited by local legislation. But the directors so acting, it was thought, were not the corporate body, but its mere agents. Wherefore, it was held, the acts of a person in the capacity of director and those of the same person in the capacity of incorporator were distinct, different; and the former could be lawfully recognized outside the state which granted the charter, but the latter could not be. A corporation, it was held, had no existence, therefore, eighteen years after the attempted acceptance of the North Carolina charter in Maryland, although all that time it had been carrying on a mining business and exercising what it supposed to be its corporate rights. This was not a case, thought the court, in which the necessary acceptance of the charter was to be presumed or inferred from the assumption and exercise of the corporate powers granted, since the proof clearly showed when, where, and how the charter was accepted. The result was that a stockholder who had brought action to be reinstated after being ousted for refusing to pay an assessment on his stock, found himself without remedy although he did not, nor had he intended, to challenge the legal existence of the corporation. It is unnecessary to do more than point out the fact that the Maryland court's strict view of the existence of foreign corporations does not indicate any tendency as yet to

yield to the modifications admitted in other jurisdictions. Nor is the finding of the court in accord with the rule that the legal existence of a corporation can only be challenged by direct proceeding by the state.

In formulating its conclusions as to the law of foreign corporations, the Maryland court adopted the strict interpretation which Chief Justice Taney had given in Bank of Augusta v. Earle some years before,—a doctrine which, in the light of necessity, has since, to a large extent, been modified and partially abandoned by the Supreme Court of the United States.[262] The law of foreign corporations, it will be remembered from the discussion of the Supreme Court decisions, contains the most conservative and least satisfactory application of the theory of the existence of a separate corporate entity. This strict interpretation is evidently reflected in Judge Miller's decision as to the jurisdiction of a court over a corporation in a county other than that in which it had its legal residence.

However this may be, subsequent acts of the legislature evidence the purpose to extend jurisdiction over corporations within the state and to facilitate the service of process. Section 296 of article 23 as it appears in the Code of 1888 was enacted by chapter 316 of the Law of 1884, which added to the section as it previously stood permission "to serve process anywhere within the state on any agent or other person in the service of such corporation, where neither the president, directors, manager, or other officers should reside in the state"; and provided that corporations other than those formed under the general law could still be sued in the place prescribed by the rule of the common law—that is, either in the place of their principal office or where they conducted their business. The amendment of 1884 only operated upon service of process. Chapter 128 of the amendment of 1884, for the same purpose of extending the service of process generally, authorized the summons wherever issued to be directed to and served by the sheriff of any county

[262] Henderson, Foreign Corporations in American Constitutional Law.

or city where the defendant may chance to be, returned to the court whence issued. It gives to such service the same effect as if made by the sheriff of the county, and in the county, where the process issued. However, it left untouched the jurisdiction over the subject-matter, and the form of the suit. The court, in discussing this question, stated that they "find nothing in the examination of the legislation on this subject which will warrant us in holding, since the enactment of the rule of construction making the word 'person' include corporation, that a corporation does not come within section 132 of article 75."

The question whether the term "person" includes corporation again came before the court on the question of jurisdiction in the case of Phillips v. the Mayor and City Council of Baltimore.[263] This time a public corporation was involved. The point at issue was whether or not such a corporation could be sued outside of its own courts upon a transitory cause of action. By the provision of article 1 of the Code, it was argued that the word "person" should include corporation in this case, inasmuch as it was believed that such a construction would not be unreasonable. The court, however, took the contrary view. A number of jurisdictional legislative acts were under consideration. One of these, the act of 1884,[264] provided that "any person who resides in one county and carries on any regular business or habitually engages in any avocation or employment in another county may be sued in either county." "Any person," however, was held not to include municipal corporations.

The precedent which seemed to have most weight with the court in determining this point was the decision in Mayor and City Council of Baltimore v. Root.[265] In that case the Act of 1825[266] was before the court. It authorized, under certain conditions, "attachments to be laid in the hands of the plaintiff or any other person or persons whatsoever, corporate or sole." The

[263] 110 Md. 432, 72 Atl. 902.
[264] Code 1904, Article 75, sec. 144.
[265] 8 Md. 103.
[266] Laws of Maryland, 1825, chap. 114.

court held that the use of the term "person" did not include municipal corporations. This case, however, and the case in 110 Maryland, in which it is cited, are not so significant in general corporation law from the point of view of the interpretation of the nature of the corporate entity as they are for the light that they throw upon the different status enjoyed by a public municipal corporation, as compared with the ordinary private corporation.

Turning now to the interpretation placed upon the word "person," as it appears in the usury provision of the state constitution,[267] we find that, in Citizens' Security Loan Company v. Uhler,[268] the court by implication assumed that the term "person" included corporation. An act passed by the legislature in 1872,[269] providing that a certain class of corporations should be exempt from the provisions of the constitution which fixed the legal rate of interest at six per cent unless the legislature should otherwise determine, was held to be unconstitutional in the following language: "The legislature has power to prescribe the rate of interest for all persons or corporations either above or below six per cent * * * but it has no power to authorize one person to charge six per cent and another ten per cent and another twenty-five per cent." From this decision Judges Alvey and Stewart dissented, but their opinion was not a dissent from the language including, by inference, corporations in the term "persons."

Summary. From the discussion of the cases in this section of the chapter, several conclusions may be drawn. A corporation, without doubt, may be an inhabitant, and have a domicile and a legal residence. This was true according to the common law of England and has not been disputed in this country. By common law rule it may reside in the place where its principal office is located or where it carries on its principal business. In the earlier periods of less extensive economic and social develop-

[267] Constitution of Maryland, art. III, sec. 57.
[268] 48 Md. 455 (1878).
[269] Laws of 1872, chap. 178.

ment of the state, these two places necessarily coincided. Later, with the development of turnpike, canal, and railroad companies, they were more often separate locations. It became necessary, as evidenced by the common law rule above quoted, to widen the rule that a person may be sued only in the county in which he resides. Not only was the forum of suit widened as to the jurisdiction over the subject-matter, but with the growth in size of the corporation and the business conducted throughout the state, a number of general acts were passed to facilitate the service of process on corporate agents.

Meanwhile, in a series of cases, including Germania v. State in 1854, the Crowther case in 1885, Maryland Home Fire Insurance Company in 1899, and Phillips v. the Mayor and City Council of Baltimore, the corporation, with the aid of the legislative Act of 1888, was received into the group of recognized "persons" in the state, and given a fixed status as such in the codified rules of interpretation of public general laws, and in the court decisions.

The corporation, however, is still regarded with some suspicion in the eyes of the Maryland Court of Appeals. As to foreign corporations, the strict view of the corporate entity obtains. As to public corporations, the public is protected by the decision that, in the case of a public municipal corporation, it would be unreasonable to include such a body within the terms of certain jurisdictional statutes. They may not be sued on a transitory cause of action outside their own courts. This finding of the court inured to the protection of the corporation itself as well as to the public. In Phillips v. Baltimore, the court distinctly recognizes the line of cases therein quoted, in which the rule of public convenience is set forth as the basis of the decisions where public municipal corporations were not permitted to be brought within the express terms of a jurisdictional statute which referred to "every person."

In the cases involving private corporations where the court has held the general law requiring two sureties on a trustee's bond inapplicable to corporations, the real reason is left to con-

jecture as to why private corporations have not been included in the term "surety." But the court has evidently looked both to the intention of the legislature in passing such an act and the nature of the corporation as a financial organization. For it is evident that the object of the general law which requires two sureties on the bond of a trustee is designed to give adequate protection to the public against financial loss by reason of the trustee's default. And the degree of financial strength thought necessary to insure such security is, evidently, in the mind of the court, to be found in the sole suretyship of a corporate security quite as much as in double suretyship on the part of individuals. By holding that the general law applies only to "personal sureties" and excludes corporations, the inference as to the financial strength of corporations is probably correct. The court, however, did not expressly adopt this reasoning. If, in the future, it should appear that corporate organization of itself does not necessarily mean greater financial strength, it is possible that the court, in the absence of further legislation, might see fit to modify its view as to the application to corporations of the general suretyship law.

As to the strict interpretation of the nature of a foreign corporation which prevails in Maryland, it may be expected that in the future, in the light of the more advanced position taken by the United States Supreme Court, the Maryland Court of Appeals will gradually modify its narrow doctrine.

Finally, it may be said that Maryland, since 1888, takes its place with the majority of the other states in including within the rules of interpretation, corporation, as coming within the meaning of the term "person," when such a meaning would not be unreasonable. The conservatism of the Court of Appeals in this respect was overcome by the more advanced position taken by the state legislature.

CHAPTER VII.

DEVELOPMENT OF THE CONCEPTION OF THE CORPORATE ENTITY IN MARYLAND LAW.

Early Cases Interpreting Corporate Existence. One of the first cases in which an analysis of the nature of the corporation is undertaken by the Maryland court is McKim v. Odom.[269x] "So far as I have been able to ascertain," said Chancellor Bland, "this is the first instance of an application to this court for a coercive process against a body politic. Corporations have latterly become very numerous, and new ones are created at almost every session of the legislature, and the matter now submitted for determination, therefore, has an importance much above the interests of the case out of which it arises, and requires to be carefully considered with a view to the court's proceeding in the future."

If it was true in 1828, when Chancellor Bland wrote this decision, that "corporations have latterly become very numerous and new ones are created at almost every session of the legislature," so that the "matter now submitted for determination has, therefore, an importance much above the interests of the case out of which it arises," it would be enlightening to examine the court's reasoning as to the nature of the corporation, which brought it to the conclusion that "a corporation cannot, in its corporate capacity, commit a crime." "It is admitted on all hands," said the court, speaking in the language of a day gone by, "that in a suit against a corporation none of its members can be taken or personally punished, except perhaps as a last resort, on account of any contumacy in their corporate capacity. The only mode of proceeding either to enforce an answer or

[269x] 3 Bland (Md. Chancery), 407 (1828), cited and annotated in 3 L. R. A., N. S. 1003.

obedience to a decree, is by a *distingas* and sequestration."[270] And, again, it was said, "the mode of proceeding against contumacious natural persons who neglect or refuse to answer, is well established, and sufficiently energetic; but the course of procedure against artificial bodies or corporations, is different, more feeble, and much more tardy, there being no legislative provisions for enforcing an appearance or answer from such defendants."[271]

It is natural that the court's difficulty in treating with the corporation should lead it to define its conception of corporate personality and existence and analyze the corporation as it existed in the first quarter of the nineteenth century, with reference to the various types then evident. This case stands out at the beginning of a long line of decisions which define corporate existence in Maryland. The careful discussion in which the learned Chancellor reviews the development of the law which he holds applicable in the state merits attention. "Under the Provincial Government," he says, "the corporations were framed and called into existence, as in England, either directly or by or with the immediate sanction of the Lord Proprietary or the Monarch."[272]

"But, however they may have originated elsewhere," said the court, "it is certain that they can now only be established here by the authority of the legislature. The multitude of bodies politic that have been created, either by the government of the Province or of the Republic, most of which still subsist, may be considered in referenec to their objects, as belonging to one or the other of three distinct classes."

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[270] 3 Bland, 420.

[271] Ibid., 416.

[272] 3 Bland, 407, 416, and note quoting 1 Black. Com. 472; and the case of Sutton's Hospital, 10 Co. 23; and Chancery Proceedings, lib. C. D., fol. 54; Incorporating Act of the City of St. Mary's (1667); Charter of Annapolis Chancery Proceedings, lib. P. C., fol. 590 (1708), ch. 7. A distinction is made between a "closed" corporation ("one in which the governing body of the city is self-perpetuating"), and an "open".

The three classes of corporations which the court then discusses correspond to the modern types of public, public-service, and private corporations. The "numerous corporations" which are mentioned as having been brought into existence by the Provincial or state legislatures were public, and, for the most part, public municipal corporations. According to our classification of corporations, says Chancellor Bland, "the first kind are such as relate merely to the public police; which, by assuming upon themselves some of the duties of the state, in partial or detailed form, and having neither powers nor property for the purposes of personal aggrandizement, can be considered in no other light than as the auxiliaries of the government of the Republic; and consequently, as the secondary and deputy trustees and servants of the people. The right to establish, alter, or abolish such corporations seems to be a principle evidently inherent in the very nature of the institutions themselves, since all mere municipal regulations must, from the nature of things, be subject to the absolute control of the government. These institutions being in their nature the auxiliaries of the government in the great business of municipal rule, cannot have the least pretension to sustain their privileges, or their existence, upon anything like a contract between them and the government; because there can be no reciprocity of stipulation; and because their objects and duties are incompatible with everything of the nature of such a compact."[273]

In his description of the powers of such public corporations, the Chancellor said: "The power of acquiring and holding property, although almost always given, is by no means a necessary incident to all corporations of this class. They may be established without any such capacity; as in the instance of the Commissioners for Emitting Bills of Credit."[274]

This treatment of the public corporation as a part of the state itself and its affairs as those of the state, is drawn from Montes-

[273] 3 Bland, 417.
[274] Maryland Laws (1769), ch. 14, s. 6.

quieu's "Espris de Lois." The Chancellor, quoting, says, the "preservation of morals, and the administration of justice, are the chief ends for which government has been instituted; and infancy, insanity, infirmity, and helpless poverty have undoubted claim upon the protecting care of the Republic."[275] Public corporations in colonial times, subserved these ends. "Bodies politic of this class, having these objects in view," said the court, "are city corporations,[276] levy courts,[277] county schools of the Provincial or state government,[278] public colleges,[279] hospitals,[280] trustees of the poor of the several counties."[281] It may be noted that today such institutions as hospitals and colleges are quite as often conducted by private corporations as by public.

The second class of corporations discussed by the Chancellor in McKim v. Odom corresponds to what today are known as ordinary private business corporations. His theory of the nature of this type, however, is somewhat indistinct, and reflects the fact that they were at the time of this decision comparatively new institutions in the country. The view here set forth does recognize the corporation as having a distinct personality, but treats it as somewhat akin to a partnership. The corporation, says the court, "is not thought to be one of the elements of society of which government is organized."

"The second class of corporations," said the court, "was such as have no concern whatever with the duties of the Republic; nor are in any manner bound to perform any acts for its benefit; but whose only objects are the personal emolument of its members. * * * The corporation in such institutions may be also mere factors of individuals; and therefore their resignation or removal cannot divest or alter any of the rights of the individuals they represented. Each member of such an aggregation

[275] Montesquieu, Spirit of Laws, b. 23, c. 29.
[276] 1708, ch. 7, and 1796, ch. 68, Laws of Maryland.
[277] Laws of Maryland, 1804, ch. 73.
[278] Ibid., 1696, ch. 17; 1723, ch. 19.
[279] Ibid., 1782, ch. 8.
[280] 1797, ch. 102; 1816, ch. 156.
[281] 1768, ch. 29; 1785, ch. 15.

either was a proprietor at the commencement, or became so during the existence of its incorporation; and consequently, must continue to be so after its dissolution. * * * A corporation not being, like a natural person, one of the elements of society, of which government is formed, can only be considered as a creature of the law. It is the law alone which gives to it a personality distinct from that of each of its members, and confers on it the right to act by its president, directors, or agents, in a manner analogous to that in which the government itself acts by its regularly constituted functionaries. This individuality of character, and the right so to act, is, then, nothing more than a portion of the power of the government with which it has been invested."[282] This seems a curious conclusion at which to arrive, after stating that these corporations have no concern whatever with the duties of the Republic. The court continues: "It is this power which is given by the creation of a body politic, and which, by its extinguishment, is resumed, and nothing more; the rights of property vested in its several members, in all other respects, remain unaffected by its dissolution."

That the modern private business corporation is a thing much more recent in origin than the concepts entertained as to its existence, is evident from the court's remark that, "It is remarkable that there is no instance of the creation of any body politic of this description under the Provincial government; but since the establishment of the Republic they have increased and multiplied to a very large and still rapidly growing family. The examples of this class of corporations are the insurance companies;[283] the Free Mason societies;[284] the banks;[285] the manufacturing companies;[286] the library companies."[287]

The third species of corporations referred to by Chancellor Bland, "partake, in many respects, of the nature of the two first

[282] 3 Bland, 418.
[283] Laws of Maryland, April, 1787, ch. 20.
[284] Ibid., 1821, ch. 147.
[285] Ibid., 1790, ch. 5.
[286] 1808, ch. 49.
[287] Ibid., 1797, ch. 35.

classes; and are such as have a concern with some of the expensive duties of the state, the trouble and charge of which are undertaken and defrayed by them, in consideration of certain emolument allowed and secured to their members. In cases of this kind there are certainly many of the material features of a contract between the government and the corporation, and there is manifestly a *'quid pro quo.'* But this contract, if it be so, is, and of necessity must be, like all others of which a government or state is a party, one of imperfect obligation as regards the state;[288] and, as such, subject to be dealt with by the government of the state as the public good may require, on making a just compensation for any private property which may be taken for a public use."[289]

Here, then, is a description of what corresponds to the class known as public-service corporations. The somewhat hazy definition of them is accounted for, as in the case of that of private corporations, by the fact that "no bodies politic of this description were ever granted under the Provincial government; but since our independence a great number of them have been called into existence; such as canal companies;[290] bridge companies;[291] turnpike road companies."[292]

Turning, now, to a consideration of the powers of corporations, the court says: "The right and capacity to sue and be sued, is an incident to bodies politic of all descriptions."[293]

As to foreign corporations, it was held that, "It is held incumbent upon every body politic, not being incorporated by a public law of which the court is bound to take notice, which comes into a court of justice as plaintiff, if required, even upon the general issue only being pleaded, to show the authority under which it

[288] Citing Vattel, Law of Nations, Prelim. s. 17.
[289] 3 Bland, 419.
[290] Laws of Maryland, 1783, ch. 23.
[291] Ibid., 1795, ch. 62.
[292] Ibid., 1797, ch. 65.
[293] Citing 1 Bl. Com. 385; 4 Com. Dig. 487; Henriques v. Dutch West. Ind. Co., 2 Ld. Raym. 1532; National Bank of St. Charles v. De Bernales, 11 Com. Law. Rep. 475.

has assumed to act as a corporation.[294] When called on as a defendant its corporate capacity is thus admitted, and it appears by attorney, and responds under its seal, or in the manner specially prescribed to it."[295] The novelty of the questions raised by these new corporate bodies is evidenced by the court's statement that "there is no legislative enactment which directs in what mode a corporation of any kind may be compelled to answer in case it should neglect or refuse to do so." And, again, the court says: "It is admitted on all hands, that in a suit against a corporation none of its members can be taken or personally punished, except, perhaps, as a last resort, on account of any contumacy in their corporate capacity. The only mode of proceeding either to enforce an answer or obedience to a decree is by a *distingas* and sequestration of property of the body politic."[296]

That the court, in this early period in the development of corporation law, sought light as to the nature of the corporation in the state as an analogous type of corporate body, appears from its statement that, "A state itself is regarded in many respects as a mere body politic,[297] and in the various instances where it becomes necessary to have it made a party to the litigation, it is represented by its Attorney General; in which case the course of the court merely allows that he should be attended with a copy of the bill; but he cannot be forced to answer in any manner whatever.[298] And, therefore, if the bill cannot be taken *pro confesso* against the state,[299] the further progress of the case must await his good pleasure."

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[294] Citing 4 Com. Dig. 487; McMechen v. Mayor of Baltimore, 2 H. & J. 41; Agnew v. Bank of Gettysburg, 2 H. & G. 479.

[295] Act of 1804, ch. 73, s. 6.

[296] Citing Bac. Abr. tit. Corporation, E. 2; Lynch v. Mechanics Bank, 13 Johns, 127.

[297] Citing Act of 1785, ch. 36.

[298] Citing Willis' Equity Plea. 7.

[299] Citing 2 Mad. Pr. Chan. 335; 1 Fowl. Exch. Pra. 401; Nabob of the Carnatic v. The East Indian Co., 1 Ves. Jun. 371; S. C. 1 Hoven. Supp. 149.

In the early English period, it had been held by the ecclesiastical courts that a corporation could not be excommunicated because, forsooth, it had no soul. This reasoning became well-settled in England. Wherefore, it was held that a corporation could not act except under corporate seal. A logical deduction from such a premise was, therefore, that no corporation could be held liable for any act not done under the corporate seal. The corporate body could not be held liable for torts and crimes. By the time Chancellor Bland wrote his decision in McKim v. Odom, however, it had become pretty well settled that a corporation could be held responsible for its acts in tort. It is the influence of this early doctrine which has persisted for generations, and it is quite probable that it still overshadows us in the hesitation by the courts to hold the corporation liable in crime. To be sure, today "mind" and "soul" have given way in the argument to "will," and it is urged that will is a product of the human mind and, since only man has a will, therefore a corporation cannot be held for a crime which requires a certain state of mind.

The discussion of this early doctrine of the soulless corporation by the Maryland court, and the fictions introduced to circumvent it, is both interesting and enlightening. "Every corporation," says the court, "must be composed of, and conducted by natural persons; yet the distinction between the natural and artificial capacities and liabilities of its members has been drawn in such a manner as to create the most serious inconvenience. A body politic, it has been quaintly said, has no soul; and therefore cannot be called on to answer under the obligation of an oath by which a natural person may be bound.[300] * * * To avoid this difficulty the Court of Chancery has had recourse to a singular shift; which, it is admitted, rests on very questionable principles; it allows the secretary, bookkeeper, or some one or more of the chief members of the body politic to be made co-defendants for the express purpose of obtaining an answer

[300] Citing Sutton's Hospital, 10 Co. 33.

on oath; which answer, contrary to the general rule in other cases, is received as evidence against the corporation itself."[301]

Here we have one of the early fictions by which the courts gradually discarded their original doctrines. They allowed the "plaintiff to select from among the corporators such one or more of them as he may think proper to make witnesses and exact from them only such proof as may be entirely responsive to his case." The use of such a fiction became too cumbersome. At the time Chancellor Bland was writing, it was "settled, that a corporation may be charged in actions *ex delicto* as well as *ex contractu,* notwithstanding the general rule that they can only act and bind themselves by means of their corporate seal. For although members of a body politic, in their corporate capacity, cannot commit a crime, or perpetuate a felony; yet since the institution is governed by the intellectual agency of natural persons, they may cause it so far to depart from the purposes of its establishment, as, by means of its servants to commit a trespass, or tort, or unlawfully to refuse to make compensation for that by which it had been, upon its own request, materially benefited. Therefore, redress is allowed to be had against it by an action of trespass, trover, or assumpsit, as may be best suited to the true nature of the case."[302]

It remained, however, for the present generation to extend this doctrine to full criminal liability, both by new legislation defining crimes broadly enough to make the crime and the penalty applicable to corporations, and by a more liberal attitude

[301] Citing Fenton v. Hughes, 7 Ves. 289; Dummer v. Corporation of Chippenhaum, 14 Ves. 253.

[302] Citing Com. Dig. tit. Franchises, F. 19; Yarborough v. Bank of England, 16 East, 6; Bank of Col. v. Patterson, 7 Cranch, 299; McDonough v. Templeman, 1 H. & J. 156; Bank of the United States v. Norwood, 1 H. & J. 423; Kennedy v. Baltimore Insurance Company, 3 H. & J. 367; Union Bank of Maryland v. Ridgley, 1 H. & G. 419.

On the point of redress against a corporation by trespass, trover, or assumpsit, cases cited are: Com. Dig. tit. Franchises, F. 19; Yarborough v. Bank of Eng., 16 East, 6; and the other cases cited in preceding paragraph.

of the courts as to the nature of the corporate entity and the purpose of its existence.

The significance of the court's description of the steps by which the early broadening of the interpretation of the nature of the corporation was attained warrants further quotation from McKim v. Odom. "The adjudications by which these modes of proceeding have been sanctioned," it was said, "manifest a sensible and strong disposition in the courts of justice so to control and modify the ancient distinction between the artificial and natural capacities of those of whom corporations may be composed, as to prevent them from withholding a disclosure of the truth; or from perpetrating wrong and fraud, under cover of their artificial capacity; because of the quaint notion that, as such, they have no soul; or because, in general, they can only act or bind themselves in the manner prescribed by means of their corporate seal."

The steps by which the courts had already done away with the rule which required all acts of the corporation to be done by corporate seal is not merely of historical interest. The discussion of that subject by the Maryland court at the very beginning of the application of established concepts to private corporations throws light upon the nature of the corporation entertained in Maryland a century ago, and at the same time points the way by which the law is in the future to broaden further. In the case of the Sable Company,[303] Chancellor Johnson said: "In forming an opinion in this case I have deemed it unnecessary to review the various decisions on how far a corporate body can contract except under the corporate seal. That subject was fully and maturely considered in the case of Bank of Columbia v. Patterson,[304] and is ably treated in the opinion of the United States Supreme Court, as delivered by Justice Story, and it was also under consideration of the Court of Appeals of this State in Kennedy v. Baltimore Insurance Company.[305] With the con-

[303] 3 Bland, 606, 611 (1823).
[304] 7 Cr. 299.
[305] 3 H. & J. 367.

clusion drawn by the Supreme Court of the United States, in delivering their opinion of the extent to which corporate bodies are bound by contracts not under the corporate seal, I concur, as well as with the position taken by the Court of Appeals of this state."

Bank of Columbia v. Patterson, *supra,* had held: "It would seem to be a sound rule of law that whenever a corporation is acting within the scope of the legitimate purposes of its institution all parol contracts made by its authorized agents are express promises of the corporation; and all duties imposed on them by law, and all benefits conferred at their request raise implied promises, for the enforcement of which an action may well lie." In the opinion of the Court of Appeals in Kennedy v. Baltimore Insurance Company, *supra,* it had been laid down that, "The position is not to be controverted that, generally, a corporate body cannot act, but by its seal; but this position cannot be extended so far as to prevent their liability from the nature of the institution; or for acts done necessarily and incidentally arising from an authority delegated by such body to their agent legally appointed."

The court takes up the rule as to the use of the seal, and says: "Anciently it seems to have been held, that corporations could not do anything without deed.[306] Afterwards the rule seems to have been relaxed, and they were, for conveniency's sake, permitted to act, in ordinary matters, without deed, as, to retain a servant, cook, or butler.[307] And gradually this relaxation widened to embrace other objects.[308] At length it seems to have been established that, though they could not contract directly, except under authority of the corporate seal, yet they might by mere vote or other corporate act, not under their corporate seal, appoint an agent, whose acts and contracts, within the scope of his authority, would be binding on the corpora-

[306] 13 H. 8, 12; 4 H. 7, 6; 7 H. 7, 9.
[307] Plow. 91, b; 2 Sand. 365.
[308] Bro., Corp. 51; 3 Salk. 191; 3 Lev. 107, and Moore, 512.

tion.[309] And the courts of equity, in this respect seeming to follow the law, have decreed a specific performance of an agreement made by a major part of a corporation, and entered in the corporate books, although not under the corporate seal.[310] The sole ground upon which such an agreement can be enforced must be the capacity of the corporation to make an unsealed contract."

The philosophy of convenience which underlay the discarding of the old rule as to the seal seems destined for continued use in the future. Its application in the Sable case, and before that time, was indicative of an increasing acceptability. Said the court: "The technical doctrine that a corporation could not contract, except under its seal, or, in other words, could not make a promise, if it ever had been fully settled, must have been productive of very great mischiefs. Indeed, as soon as the doctrine was established that its regularly appointed agents could contract in their own name without a seal, it was impossible to support it, for otherwise the party who trusted in such a contract would be without remedy against the corporation. Accordingly, it would seem to be a sound rule of law that, wherever a corporation is acting within the scope of the legitimate purposes of its institution, all parol contracts made by its authorized agents are express promises of the corporation, and all duties imposed on them by law and all benefits conferred at their request, raise an implied promise, for the enforcement of which an action may well lie."[311]

Some twenty-five years later, the court again had occasion to interpret the scope and method of corporate action, and again widened its view. In Elysville Manufacturing Company v.

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[309] Rex v. Biggs, 3 P. Wms. 419.

[310] 1 Fonb. 305, Phil. Ed., Note (o).

[311] Bank of England v. Moffat, 3 Bro. Ch. Rep. 262; Rex v. Bank of England, Doug. 524, and note; Gray v. Portland Bank, 3 Mass. Rep. 364; Worcester Turnpike Corporation, Willard, 5 and 80; Gilmore v. Pope, 5 Mass. Rep. 491; Andover and Medford Turnpike Corporation v. Gould, 6 Mass. Rep. 40.

Okisko Company,[312] the validity of the subscription by the Elysville Manufacturing Company to twenty-five hundred shares of Okisko Company stock was attacked on the ground that the President of the Elysville Company had not been given authority by the corporation acting under seal, or even by express vote or resolution. In deciding the point, Chancellor Johnson had occasion again to discuss the nature of the corporation with regard particularly to its powers and methods of action. "In urging the first objection" (it was said) "that a corporation aggregate must act collectively and by vote or resolution." "But," said the court, "though this may be true, it is now well settled in this country, that the acts of a corporation evidenced by a vote, written or unwritten, are as completely binding upon it as the most solemn acts done under the corporate seal; and that promises and engagements may as well be implied from its acts and the acts of its agents, as if it were an individual."

With reference to the use of the corporate seal, Chief Judge Buchanan, in Union Bank v. Ridgley, said: "It is suggested that the use of the seal grew out of the state of the times in which it originated, when seals were more common, and better known, than signatures, and the authentication of instruments by the seals was more certain, and attended with fewer difficulties and perplexities, than any other mode of authentication; and that the use of the seal is only dispensed with, because writing may now be proved with as much certainty as the common seal.

"But that would seem to be a mistake," said the court, "in that the greater facility and certainty attending the authentication of an instrument by the use of the common seal, was not the reason why it was originally held that corporations could act in no other way. It would have been a very good reason for preferring the use of the seal to any other less certain mode

[312] 1 Md. Ch. 392 (1849), citing Bank v. Ridgley, 1 H. & G. 426, and Burgess v. Pue, 2 Gill, 254.

of authentication, but not a sufficient reason for rejecting all other modes; nor does it appear that the rule was originally introduced for that reason.

"Blackstone, in his commentaries,[313] says: 'A corporation being an invisible body, cannot manifest its intentions by any personal act or oral discourse. It therefore only acts and speaks by its common seal. For though the particular members may express their private consents to any acts, by words or signing their names, yet that does not bind the corporation; it is the fixing the seal, and that only, which unites the several assents of the individuals who compose the community, and makes one joint assent of the whole.'

"It was not, therefore," says the Maryland court, "as a mere rule of evidence that the common seal was required because more certain and more susceptible of proof than a writing or any other mode of authentication; but because it was supposed that a corporation, being an invisible body, it was incapable of manifesting its intentions, by any personal act or oral discourse; and that having neither hand nor mouth, it could no more write than speak.

"But as some mode of action was necessary to its operations, the common seal which is incident to a corporation was resorted to as an artificial representation; embodied in which shape, it could alone appear,—the hand and mouth of the corporation, by which only it was permitted to act or speak. This technical nicety has, however, gradually given away to the public convenience, and the attenuated notion that the seal only was capable of uniting the several assents of the individuals composing the community, and making one joint assent of the whole, has yielded to the sober sense of mankind, which no longer delights in mere technicalities. Yet the character and constitution of corporations remaining the same, and the united assents of the individuals composing the community being as necessary now as formerly, to constitute the act of a corporation, their assent

[313] Blackstone, Commentaries, Vol. 1, p. 475.

must be proved in some way. But by what law or on what principle has writing been substituted for the common seal and had imparted to it the magical power which it did not formerly possess, of uniting the several assents of the different individuals who compose the community? Let it be borne in mind," the court admonishes, "that at the time when the seal was alone held to be capable of performing that office, writing was necessary to show to what it was the seal did unite the several assents of the individual corporators. But the writing alone was nothing; it had no agency in manifesting the assent of the corporation, it was the thing only assented to, and the seal it was, appended to it, that spoke the persons of the corporation and manifested its assent. If there be any law substituting writing for the common seal, and declaring it to be the only means by which the assent of a corporation can be manifested," the court concluded, "it has not been produced, and we know of none such; or if there be any decisive authorities establishing that position, they have not been referred to."

Thus far, in the early decisions of the courts in Maryland, we have seen, on the one hand, the recognition of a separate corporate entity with increasing responsibility, and, on the other hand, a restrictive interpretation of the fiction that the entity exists separate and apart from its members. With the perspective of these early statements of Maryland law, we may now consider how these theories have fared in later decisions.

The Extent to Which the Courts Ignore Legal Informalities in Order to Uphold the Separate Corporate Entity: Estoppel and the De Facto Theory of Corporate Existence. The efforts of the courts to do substantial justice has led to the use of the doctrines of notice and estoppel. In the cases discussed in Chapter V there has been presented an analysis of the principles of these doctrines in cases decided by the Supreme Court of the United States. In those cases they were utilized to attribute to the corporation knowl-

edge or notice of its stockholders as agents for particular purposes, to prevent the corporation or its principal from perpetrating fraud. In none of those cases, however, was the actual legal existence of the corporation questioned by any party to the suit or by the courts which looked beyond the corporate entity.

In the cases now to be considered, corporations have assumed to act as legally existent bodies with full sanction of the creative act of the state, but they have not in fact met all of the legal requirements of the enabling statute. In such cases the question arises: Will the courts, following their rule of strict construction, disregard the corporate entity and deny it existence because it has not complied with all the requirements of the law? In other words, will the failure of the corporation strictly to comply with all conditions precedent set forth in the enabling act cause the courts to ignore the corporate body on the ground that it has never come into legal existence?

In Maryland law, probably there are no more vexed questions than those pertaining to the birth of the corporate entity. Under the revised Corporation Act of 1908, and its subsequent amendments, the old method of creation of corporations was left unchanged. In order to secure a valid charter, the essential acts, except as to certain special classes of corporations, are, first, the payment of a bonus tax, and, second, the filing of a certificate giving the name and principal office, authorized capital stock, the purposes, the names of the incorporators and directors, etc., certified by a judge to be in conformity with the provisions of the law.[314]

It must be borne in mind that there are two classes of conditions precedent to the legal existence of a corporation: first, those which the courts hold to be "indispensable" to legal corporate existence, and, second, those which are not "indispensable." Failure of the corporate body to perform a condition of the first class, as the courts hold, excludes it from the possibility

[314] Acts of 1908, ch. 240, secs. 4 and 5; 1914, ch. 789, secs. 4 and 5.

of legal birth, but failure to perform one of the second class does not. The law requires a "substantial compliance" with the creating act. Failure to perform a condition precedent of the first class precludes the possibility of such "substantial performance," in the eyes of the law. And deliberate failure or refusal to comply with one of the second class may do so, but an attempt in good faith to comply with one of the second class will not prevent the legal birth of the corporation. Even in this last situation, however, the state may question its legal right to act, if it so chooses. But in case of a substantial performance of a condition precedent of the second class the courts have accorded recognition to the corporation and granted it legal existence in all its relations to other persons.

The doctrine of estoppel is used as a means to that end, and it will be seen, from a comparison of the cases cited in Chapter V with those referred to in the following discussion, that the doctrine is employed in the former to prevent the setting up of the separate entity as an insulator between the corporation and its stockholders. In the cases now presented, however, the doctrine of estoppel is used, not to deny the separate existence of the corporate entity but to prevent its being brushed aside by members of the corporation or those who have dealt with it, in order to relieve themselves of liability. In both cases the courts look beyond the mere entity itself; but in the situations presented in Chapter V they do so for the purpose of preventing a corporation once established from becoming a cloak for fraud, and deny that the separate existence of the entity means an absolute lack of contact with its members, while in the cases herein considered estoppel is used to prevent the corporate entity from being ignored because of some irregularities in its formation.

This attitude has been affirmatively endorsed by the legislature. The Maryland Corporation Act of 1908[315] provided that, "No certificate of incorporation shall be declared void for formal

[315] Laws of Maryland, 1908, ch. 240, sec. 6.

defects merely; and where the effort has been made in good faith to form, under the laws of this state, a corporation formable thereunder, neither party to any transaction with it shall deny the legality of its incorporation or organization in any suit or proceeding growing out of such transaction; and 'transaction' shall include any wrong to person or property giving rise to a cause of action or equitable relief by or against such corporation."[816]

It should be noted that, from the point of view of the administration of justice, the alternative for ignoring the corporate entity by failure to apply the estoppel doctrine would not be to allow the individual members of the corporation to be held. The court would have no choice but to grant to persons who have dealt in good faith with the supposed corporation no remedy at all. In both proceedings, the object of the judicial tribunal in looking through the corporate entity is to prevent injustice and do justice, as best they may under the circumstances presented to them, whether it be by looking beyond a legally existent corporation, on the one hand, or preventing a group that has dealt as a corporation from denying its existence, on the other.

In conjunction with the discussion of the Maryland decisions in the following discussion it will be useful, for purposes of comparison, to note the decisions of the United States Supreme Court.

The principle of estoppel as applied by the court to prevent a group from denying legal corporate existence has been crystallized into the rule of *"de facto"* corporate existence. The United States Supreme Court has stated the principle in terms identical to the law as it is set forth in the decisions of the Maryland Court of Appeals. In Tulare District v. Shepard the *de facto* corporation is described as follows: "Where there is a special or general law under which pretended corporations might have

[816] For a discussion of Maryland cases on this point see foot note of Brady, Maryland Corporation Law, p. 94 (1914).

been formed; an attempt in good faith to organize thereunder, and an actual user of the corporate franchises, then you have a corporation *de facto,* and until the state questions its existence, no one may."[317]

Prior to the passage of the Revised Corporation Act of 1908, the Maryland Court of Appeals refused to recognize the doctrine of *de facto* existence of corporations and never completely adopted the estoppel theory.[318] Since that act was adopted the case of National Shutter Bar Company v. Zimmerman[319] has held that a corporation cannot be created by estoppel, and that the above provision was not intended to cover cases where, through neglect, there had not been any attempt to comply with the important requirements of the law. It was there held that the payment of the bonus tax is an absolute condition prerequisite to the beginning of corporate existence. Certain defects of corporate organization, however, may be cured by legislative recognition of the corporation.[320]

By the *de facto* doctrine of corporate existence, one who deals with a *de facto* corporation is estopped to deny its existence. It may be repeated, that estoppel in this sense should not be confused with the preceding discussion of the extent to which the courts will disregard the fiction theory of the separate entity and deal with the individual members. In both cases the doctrine of estoppel is used, but for a different purpose. The *de facto* doctrine is employed for the benefit both of the corporation itself and of those who contract or deal with the body in the full belief that it constitutes a corporation legally endowed with the powers it presumes to exercise. This benefits the corporations by freeing them from liability to collateral attack upon the legality of their existence. It grants them full cor-

[317] 185 U. S. 14. See also France, Principles of Corporation Law, 2nd ed., 1914; and Harvard Law Review, xxv, 623.

[318] Boyce v. Trustees, 46 Md. 359; Brady, Maryland Corporation Law, p. 94, foot note.

[319] 110 Md. 313 (1909).

[320] Murphy v. Wheatley, 102 Md. 501 (1906); Munich Reinsurance Company v. United Surety Company, 113 Md. 200.

porate powers in spite of the fact that they have failed in some formal matter to meet the law's requirements. In the *de facto* doctrine, it may therefore be said, estoppel is used to establish in full power a corporation whose legal origin is doubtful but may be questioned only in direct proceedings by the state. Moreover, the *de facto* doctrine does not apply to groups who fail to comply with what the state regards as a substantial performance of a condition precedent.

Estoppel Collaterally to Deny Corporate Existence. The principle which prohibits a defense to an action on a contract performed on one side, by collateral attack upon the legality of corporate life because the corporation's act is contrary to law, is a somewhat similar use of estoppel. Here, there is no question of the legal validity of the formal creation of the corporation. Nor is there necessarily any relation of agency as between the corporation whose right to exist is challenged and some other individual or group. A recent case before the United States Supreme Court is in point. In Wilder Manufacturing Company v. Corn Products Refining Company,[321] for instance, a refining company sued a manufacturing company to recover the price of sugar bought and consumed. The defense of the manufacturing company was that the refining company was an illegal combination in violation of the Anti-Trust Act. It was granted that an interstate transaction was involved. The court held that a collateral attack upon the legality of existence of a corporation, given the contract of sale in itself valid, is not permissible, first, as a matter of general law, and, second, because it is in violation of the express provisions of the Sherman Act granting power to the Attorney General alone to prosecute illegal combinations under the act. The court said:

"It is an elementary proposition that courts may not refuse to enforce the otherwise legal contract because of some indirect benefit a wrongdoer which would be afforded from doing so,

[321] 236 U. S. 165 (1915)—Error to the Court of Appeals of Georgia.

or some remote aid to the accomplishment of a wrong which might possibly result,—principles of such universal acceptance that no citation of authority is needed to demonstrate their existence, especially in view of the express ruling in 184 U. S. 54."

This opinion is quoted because there is danger of confusing such a case with those in which the question of disregarding the theory of the existence of the separate corporate entity is involved. Such a case as the above does not raise the latter question at all, though the principle of estoppel is used in both. The real point there involved is the forfeiture of corporate life because of the illegal act of the corporation, and the question is raised, at whose instance and when may forfeiture be effected? One who deals with the corporation is said to be estopped from denying its legal existence for the purpose of securing a forfeiture of its charter. The state only can exact that penalty.

There is a field, however, in which the doctrine of estoppel is applied in a manner similar to its use in the *de facto* doctrine when the question at issue is the right to deny the legal birth of a body corporate. Although the members may have acted in the group name and for the collective benefit, yet they may not have met the requirements of the law that would give them legal birth for the purposes of *de facto* existence, though they may themselves think they are a corporation and hold themselves out as such. If the *de facto* doctrine were interpreted in a broader sense, there would be no need for invoking such a use of the principle of estoppel as is here required. But an adherence to the *de facto* doctrine and a denial of the application of estoppel in cases where bodies of individuals have failed to conform substantially to the incorporation laws, though it be by mere oversight or carelessness, certainly works injustice upon the innocent third parties. And while it may be consistent with the old theory of the law that a corporate body is one of strictly limited powers and incapable of performing acts except in the exercise of those powers specifically granted to it in its charter, or necessarily incident thereto, yet the denial of the application

of the doctrine of estoppel to prevent the defense of *"nul tiel* corporation" in cases where the *de facto* doctrine does not apply, and refusal to sanction the acts of a body of men conducting themselves as though they were a corporation, is contrary to the more advanced and reasonable position assumed by courts of other states. By the latter it is forcibly said that disregard for such a corporate entity will not be denied in the interests of substantial justice. And it is submitted that public policy does not require that the state and the public be "protected" from bodies of persons who set themselves up as corporations, to the extent that the courts must close their eyes to what in fact is a binding contract, conceived in good faith for all purposes for which the minds and wills and understandings of the contracting parties could ever have met. Is it to be said that it is against public policy for the courts to "give life" to a body of men by recognizing their acts as creating legal duties and obligations, because the legislature has not given full legal sanction to the corporate existence of that body? Substantial justice points one way only in such cases. The corporate entity should be granted full recognition as a reality in law, as its group dealings have borne evidence of its reality in fact, even though such a body might have to bear the stigma of "illegitimate birth." The *de facto* doctrine is consistent and a convenient rule of law—but it is not broad enough to do substantial justice in the largest possible number of cases.[322]

A discussion of the Maryland case to which I have referred, Shutter Bar Company v. Zimmerman,[323] will serve as an illustration of what has been said. As a matter of logical reasoning, there is nothing inherently wrong in the court's decision. Given

[322] Typical results of this de facto doctrine and suggestions as to the need for a broader use of estoppel based on the recognition of the corporate entity as in itself a reality, are found in Boyce v. Church, 46 Md. 369; Smith v. Silver Valley Mining Co., 64 Md. 94; and compare Cannon v. Brush Electric Co., 96 Md. 446; Bonaparte v. Railroad Co., 75 Md. 215; Cleveland v. Mullen, 96 Md. 605; Isaac v. Emory, 64 Md. 333, compared with Jones v. Linden Bldg. Assn., 79 Md. 73.

[323] 110 Md. 314.

the *de facto* doctrine, it is the Maryland legislation and the failure of the court to make a broader application of estoppel that produce injustice. Judge Schmucker, who wrote the opinion, interpreted the law as the court believed it to exist on the statute books.[324] He said: "A *de facto* corporation can never be recognized in violation of positive law." And since the court understood itself to be committed to the *de facto* doctrine, it is a correct statement of the law that, "The doctrine of estoppel cannot be successfully invoked unless the corporation has at least a *de facto* existence." In the opinion of the court, the provision of the Code under consideration made certain purely formal matters "substantial" in law, and absolute conditions precedent to the exercise of corporate life or powers. As a result the court was bound to such a narrow interpretation under the *de facto* doctrine, as to what is a "substantial compliance with the law," that the only way it could possibly do substantial justice in the future would be to apply the estoppel doctrine in its broader sense.

The court does not always adhere so literally to the terms of such a statute. Take, for instance, the very much more liberal attitude adopted in interpreting the positive provisions of the statute which deals with forfeiture of the charter for failure to pay a franchise tax. In Murphy v. Wheatley[325] the question came before the court as to the interpretation of an act of the legislature which provided that, "All corporations hereafter chartered under any of the laws of this state * * * which have not within two years from the time of the grant of their charter certificates actually organized and begun business, shall be conclusively presumed to have surrendered all corporate or charter rights, unless within six months from the first day of June," etc., "each of the said corporations pay to the Treasurer of the state a franchise tax."[326] The court, however, held, through Judge Boyd, speaking, that, "Failure to pay the fran-

[324] Code, Art. 81, Sec. 98, as cited in 1909.
[325] 102 Md. 501 (1906).
[326] Laws of Maryland, 1900, ch. 272.

chise tax * * * did not cause the corporate or charter rights of the trust company to be *ipso facto* forfeited, and hence stockholders are not relieved from liability to the depositors and creditors by reason of that tax not being paid."

In discussing the reasons of the court for so liberally construing a statute which in positive language declared that, upon failure to pay the tax, there would result an *ipso facto* forfeiture, the court said: "A clear distinction is made by the authorities between acts of corporations required to be done as conditions precedent to their coming into existence, and those that cause forfeiture of charter rights and powers, after they are legally and validly acquired." The Maryland cases on the subject of forfeiture[327] are then discussed by the court. At the conclusion it was said: "We have thus referred at length to our own cases to show the position this court has taken by an unbroken line of decisions, where the corporation was an existing, valid corporation, and a forfeiture was claimed to have been incurred. And the Supreme Court of the United States in dealing with a Maryland corporation adopted the same view."

Apart from precedent, however, the reasoning of the court was as follows: "It is true that in Nicolai v. Maryland Agricultural Association[328] we said, 'There can be no doubt that the legislature may use such language in a charter as will make a forfeiture clause self-executing, and the corporation will *ipso facto* cease to exist, but it requires strong and unmistakable language to work such results.' In the construction of clauses prescribing a condition or contingency, the courts seem generally opposed to that view which supports a forfeiture *ipso facto*

[327] Canal Co. v. Rd. Co., 4 G. & J. 1, in which the 18th section of the charter of the Potomac Company was under consideration by Chief Judge Buchanan; Planters Bank v. Bank of Alexandria, 10 G. & J. 356; Hammond v. Strauss, 53 Md. 15; Musgrave v. Morrison, 54 Md. 166; Hodges v. Ry. Co., 58 Md. 623; Bonaparte v. R. R. Co., 75 Md. 348; Md. Tube Works v. West End Improvement Co., 87 Md. 207; Nicolai v. Md. Ag. Assn., 96 Md. 330; Frost's Lessee v. Frostburg Coal Co., 24 How. (U. S.), 278.

[328] 96 Md. 330.

without judgment of dissolution in a court proceeding."[329] Later in the opinion the court said: "There are numerous decisions in this state to the effect that no cause for forfeiture of a corporation which has actually come into existence can be taken advantage of or enforced against the corporation collectively or individually in any other mode than by a direct proceeding instituted for that purpose. It must be admitted that the expression used in section 85A, quoted above, is very broad, but not more so than the language referred to in Canal Company v. Railroad, *supra,* or in Planters Bank v. Bank of Alexandria, or in Frost's Lessee v. Frostburg Coal Company."

Enough of this opinion has been quoted to show that there is a marked distinction drawn by the Maryland court between the breadth of interpretation to be accorded conditions subsequent and conditions precedent to corporate existence. It is submitted that a greater degree of justice would be attained by applying a more liberal interpretation to conditions precedent. Let there be no conditions absolutely prerequisite to the legal birth of corporations except want of good faith or fraud, and let failure to comply with such conditions simply lay the corporation open to the possibility of a direct challenge to its existence by the state alone. If payment of the bonus tax must be regarded as a condition precedent, rather than, as in the case of the non-payment of the franchise tax, a condition subsequent, then let the same reasoning apply to the failure to comply with such a condition precedent as the court now applies to failure to meet a condition subsequent, and a situation more in accord with justice and convenience will be attained.

Especially is this true of a group of persons who, though having failed to meet a requisite condition precedent, have carried on business as a corporation, acquired rights and incurred obligations which cannot be set at naught with any less inconvenience, hardship, and injustice than can those vested rights and

[329] 9 Encyclopedia of Law, 555.

interests acquired by a legally existing corporation whose charter it is sought to annul.

However, in this matter of liberal interpretation of conditions subsequent, the Maryland court has taken a more advanced position than a number of the other courts. Said Judge Boyd: "We are aware that many of the courts have announced a different doctrine on the subject, from that adopted in this state. Judge Thompson, in his article on Corporations in 10 Cyc. p. 1270, says, 'Although it has been frequently said that there are four ways in which corporations may be dissolved, yet on a little reflection, it appears that there are five ways.'" And Judge Thompson states them as: first, by the expiration of the term of existence granted; second, by an act of the legislature, where the power has been reserved; third, by a surrender of its franchises which is accepted, and a valid dissolution; fourth, by loss of all its members, or of an integral part; fifth, by a forfeiture of its franchises by a judicial proceeding, usually an information in the nature of a writ of *quo warranto,* under the operations of statutes, and a proceeding in a court of equity which winds up the corporation and distributes its assets. "On the question of *ipso facto* forfeitures," said Judge Boyd, "it is evident that he is not altogether in accord with the Maryland doctrine. But with the greatest respect for the views of others, we believe that doctrine that has prevailed in this state for three-quarters of a century a safer one, and have no desire to depart from it. The business of this state—large and small—is now done so largely by corporations that it behooves courts not to encourage such conditions as are likely to arise at any time, if the views contended for by the appellees are to be sustained."

This is an admirable viewpoint, and it is believed that the court may at some time in the future modify its stricter view as to conditions precedent to more nearly conform to this doctrine. In so doing, it is true, it would be abandoning the construction of that part of the fiction of the nature of the corporation which holds that it is "merely the creature of the state,"

and would adopt the broader view which would strike out the word "merely" and substitute for "creature" the term "subject."

The reasonableness of thus broadening the field of application of estoppel is the more evident from a consideration of the manner in which the courts now deal with corporate torts. The responsibility of the corporation in tort and crime certainly was not the outgrowth of the "fiction of corporate existence" which regarded the law as the only and absolute source of the powers of the corporate body. The law never did sanction any act that was of itself a tort or a crime and the state could not be presumed to have granted any such power to a corporation. The necessity of recognizing the facts of ordinary business experience brought about this revolution in the conception of the entity with reference to its liabilities and obligations.

Forty years ago, in Carter v. Howe Machine Company,[330] Judge Alvey took the advanced position that, whatever may have been the former state of judicial opinion upon the subject, today "corporations are liable for all acts, whether willful or malicious, of their agents or servants, done in the course of their employment. Hence it has been repeatedly decided that corporations are liable in actions for assault and battery, and false imprisonment, committed by their servants, and for false representation, and for libel, as well as for all consequences of the negligent or unskillful acts of their servants, within the scope and course of their employment; and it would appear that actions for such injuries may be maintained against a corporation aggregate in any case where, under similar circumstances, such acts may be maintained against individuals for the acts of their servants."[331]

Referring to the cases cited in the last note, the court said: "The first two of these cases were actions for libel and the two last, for assaults and false imprisonment. If such actions, founded on wrongful acts done intentionally, without just cause

[330] 51 Md. 290 (1878).

[331] Citing Philadelphia, Wilmington and Baltimore Rd. Co. v. Quigley, 21 How. 202; and El. Bl. & E. 121; 6 Exch. 314; 3 El. & El. 672.

or excuse (the requisite elements of legal 'malice'), can be sustained, why should there be any difficulty in sustaining the action for malicious prosecution?[332] * * * In this conflict of authority it would seem that the question has been regarded as one not free from difficulty. But, upon the whole, we quite agree with Judge Cooley, that for the same reason that actions for libel or for false imprisonment may be maintained against a corporation, an action for malicious prosecution may be maintained against it. They all alike involve the element of malice, and this court has held upon more than one occasion that express malice or malice in fact may be imputed to a corporation for the willful and violent acts of its servants in the course of their employment.[333] And for all acts done within the scope of the employment and the limits of the implied authority, the master is liable, however erroneous, mistaken or malicious such acts may be; but for acts done beyond that limit the corporation cannot be made liable, unless express authority be shown, or there be subsequent adoption or ratification of the act complained of." This is a remarkably clear and a decidedly advanced position that the court has taken as to corporate liability in tort. It is submitted that there is no valid reason why the same reasoning should not be extended in the future to corporate liability for crime.

Two years before Judge Alvey's decision in Carter v. Howe Machine Company, Judge Stewart had voiced the opinion of the court in Baltimore and Yorktown Turnpike Company v. Boone,[334] that a corporation is capable of deliberation in the contemplation of the commission of an injury. That case involved liability for the expulsion of a passenger from the car of a public service corporation, and the determination of the

[332] Citing Cooley, sec. 121; Vance v. Erie Rd. Co., 32 N. J. 334; Goodspeed v. E. Haddam Bk., 22 Conn. 530; Copley v. Sewing Machine Co., 2 Woods (U. S. C. C.), 494; Fenon v. Sewing Machine Co., 9 Phil. (Penn.), 189; Walker v. S. E. Ry. Co., L. R., 5 C. P. 640.

[333] Citing B. & O. Rd. Co. v. Blocker, 27 Md. 287; Balto. & Yorktown Turnpike Co. v. Boone, 45 Md. 334.

[334] 45 Md. 344.

court placed a greater degree of responsibility and guilt upon the corporate body than would have been attributed to an individual in similar circumstances. In its opinion, the court announced that, "Force, fraud, malice, wantonness, rudeness, oppression, gross negligence, or deliberation, inexcusable or criminal indifference to civil obligations or the rights of others, may all be ingredients in the acts complained of. It was said in very concise language, in the decision of the Supreme Court in Philadelphia, Wilmington, and Baltimore Railway v. Quigley, [335] that whenever the injury complained of has been committed wantonly or maliciously, and with circumstances of contumely or indignity, the jury is not limited to the ascertainment of a simple compensation for the wrong against the aggrieved party.

"But the malice is not merely the doing of an unlawful or injurious act; the word implies that the act was conceived in the spirit of mischief or of criminal indifference to civil obligations.

"Such indifference to the obligations of public duty on the part of a corporation created not solely for its own emolument, but for the public convenience, may afford reasonable ground of liability for exemplary damages."[336] * * * "The defendant, upon whom corporate franchises had been conferred, must be presumed," said the court, "in the absence of any evidence to the contrary, to have acted advisedly and with full deliberation, in regard to its dealings and transactions with the public. An individual committing a similar act might not ordinarily be considered as having the same means and inducements for deliberation in his conduct, nor affected by the same sort of liability and obligation."

It is wholly consistent, then, with the conception of the corporation taken by the Court of Appeals of Maryland, as a real and distinct entity, to broaden the estoppel doctrine in its appli-

[335] 21 How. 214.

[336] Two necessary elements of the tort involved are deliberation and force.

cation to conditions precedent. It is submitted that the statement of the law made by the Maryland Court of Appeals in the case of Boyce v. Church[337] that, "We think it would be extending the doctrine of estoppel to an extent not justified by the principles of public policy to allow it to operate through the conduct of the parties concerned to create substantially a *de facto* corporation, with just such powers as the parties may by their acts give it," is not now, after forty years of tremendous expansion in corporate industrial and financial enterprise, consistent with the administration of substantial justice in the majority of cases. Should the court adopt the attitude that parties dealing with the corporation are estopped to deny collaterally its compliance with a condition precedent, more substantial justice would be done.

We do, however, agree with the court's remark, in the Boyce case, that "It would be more reasonable to hold corporations to their contracts, though *ultra vires,* of which they have received the benefit, or to prevent parties who have contracted with them, and received the benefit therefrom, from defeating their liability, on the ground of want of power in the corporations, as is held in quaretrs of high authority,[338] than to hold that corporations should be deemed to have existence, because they had so held themselves out." The Maryland court, however, does neither. Substantial justice requires both. It is to be regretted that the court has not seen fit to follow this suggestion even in the cases in which *ultra vires* acts are concerned. In the late case of Western Maryland Railroad Company v. Blue Mountain Company, [339] that tribunal still refuses to apply the estoppel doctrine to *ultra vires* acts.

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[337] 46 Md. 359, 373 (1877).

[338] 2 Kent, 351.

[339] 102 Md. 307 (1905). See also Steam Navigation Co. v. Dandridge, 8 G. & J. 254 (1836); Maryland Hospital v. Foreman, 29 Md. 524 (1868); Wekler v. Bank, 42 Md. 582 (1875); Lazear v. Bank, 52 Md. 78 (1879); Booth v. Robinson, 55 Md. (1881); Bank v. Katz, 57 Md. 128; Heirominus v. Sweeney, 83 Md. 146 (1903).

It should be noted that estoppel in *ultra vires* acts has but an indirect bearing upon the question of the extent to which the courts will disregard the irregularities of corporate formation to support the existence of the entity, or to the question of the extent to which the courts will disregard the fiction of corporate existence and deal with the individual members. It is evident from a consideration of the nature of *ultra vires* acts and the rulings of the United States Supreme Court[340] and the Maryland Court of Appeals, that the theory upon which the strict rule is based, namely, that a contract in excess of granted powers is one which the corporation is incapable of making, is a direct outgrowth of the old, narrow, strictly limiting theory of the corporate entity as incapable of exercising in fact powers other than the state specifically grants. It is not, like the doctrine of estoppel in the *de facto* doctrine of corporate existence, concerned with the legal birth of the corporate body. It admits legal existence. But it concerns itself with keeping the corporate acts inside the strict confines of state-granted charter powers. It has its eyes narrowly fixed on the fiction of the corporate entity as a creature of limited powers only. It does not recognize the fact that individuals do act as a collective unit though not technically incorporated according to law, nor does it see that a technically incorporated body in fact does overstep its charter right at times, and acts, sometimes in good faith, beyond the scope of its legal powers.

The United States Supreme Court, in its zeal to protect the separate entity, on the one hand, and, on the other hand, to confine the corporate acts strictly within the charter grant of power, has underemphasized the more balanced justice that might result (particularly as to innocent third parties) if the doctrine of estoppel were more liberally applied in giving effect

[340] Central Transportation Co. v. Pullman Co., 139 U. S. 60. See Digest of U. S. Reports, sub-head, Ultra Vires.

[341] R. R. Co. v. Keokuk, 131 U. S. 371; McCormick v. Bank, 165 U. S. 550. In 130 U. S. 1, the court said that a contract *ultra vires*, although assented to by all the stockholders, is void.

to *ultra vires* contracts.[341] It does not appeal to reason to expect all persons who contract with a corporation to have knowledge of the extent of the charter powers of each particular corporation with whom they deal.[342]

Neither has the Maryland Court of Appeals, in the case of Western Maryland Railroad Company v. Blue Mountain Company seen fit to break away from the strict rule. To hold that the contract of a railroad company which has guaranteed the bonds of a hotel company is void because *ultra vires* as to the railroad company, and that, since an accounting, or action for moneys had and received, is the only remedy recognized by the law in its present condition, there can be no remedy for the hotel company because "the proof is clear that the railroad company never received from the hotel company, either directly or indirectly, any money or property whatever under its contract,"[343] can hardly be said to be in accord with substantial justice. It was not denied that the hotel company acted in good faith in the performance of its part of the contract in building the hotel. Nor, as a matter of fact, could it be denied that the railroad company received the benefit by way of performance of a contract obligation.

This is a striking case in which the denial of the application of estoppel to an *ultra vires* contract worked injustice to an innocent third party,—the holder of the bonds of the hotel company. Had the court applied the doctrine of the case of Steam Navigation Company v. Dandridge,[344] that "parties may be

[342] In R. R. Co. v. Keokuk, etc., Co., 131 U. S. 371, the court said: "The reasons why a corporation is not liable upon a contract *ultra vires*, that is to say, beyond the powers conferred upon it by the Legislature and varying from the objects of its creation as declared in the law of its organization are: First, the interest of the public that the corporation shall not transcend the powers granted; second, that the capital stock shall not be subjected to the risk of enterprises not contemplated by the charter and therefore not authorized by the stockholders in subscribing for the stock; third, the obligation of every one entering into a contract with a corporation to take notice of the legal limits of its powers."

[343] 102 Md. 307, 335.

[344] 8 G. & J. 248, 319, quoted in 102 Md. 333.

estopped in some places from disputing the validity of a corporate contract when it has been fully performed" on one side and "when nothing short of enforcement will do justice," the decision would have been more in line with the tendency of other courts to recognize the corporate body as a legally responsible entity and accord recognition to its acts *ultra vires* as well as *non ultra vires,* for the purpose of doing justice.

There seems to be a commendably heterodox doctrine growing up, however, in some jurisdictions. In the leading case of G. V. B. Manufacturing Company v. First National Bank of Harley,[345] the principle was stated, that "When the business of a corporation is conducted in an irregular manner and the contracts have thus been made with shareholders by one acting *bona fide,* with knowledge of the corporation's methods of doing business, the ordinary rules * * * as to powers of officers, * * * fail to apply and the corporation will be bound."

In that case, the president of a corporation had been permitted to exercise full power in the conduct and management of its business, and had dealt with the property and officers of the corporation in such a manner and for such a length of time as to justify others with whom he transacted business in believing that he had authority to do the acts in the manner in which they had been done. It was held that such third persons had a right to deal with him on the assumption that he had such authority, and the corporation, having knowledge of such acts, and of the manner in which the corporate business was transacted, could not thereafter, to the injury and prejudice of the third persons, deny the president's authority or disaffirm his acts.

Estoppel and One Man Corporations. The so-called one-man corporation, in which a single individual, either in person or as principal, becomes owner of all the stock, intro-

[345] 95 Fed. 23; and see 82 N. J. L. 557, 82 Atl. 854, holding that when shareholders perform acts normally performed by directors and in the regular course of business, their acts bind the corporation; 96 Wis. 317, 71 N. W. 652; 79 Fed. 828; 10 Cyc. 760, 936.

duces no really new problems into the law of corporations. It offers a somewhat more puzzling situation, to be sure. But there is still a clear distinction between corporate acts and the acts of the sole owner in his individual capacity; and between the corporate property and the property of the individual. The principles which should control are the same as those in cases above noted where a corporation is merely the agent of the individual. As noted in the discussion in Chapter V, if a corporation owns all the stock of a subsidiary company, the courts do not hesitate to set aside the defence of separate corporate entity when set up by the dominant corporation that owns the stock, if the subsidiary corporation be used to commit a fraud or breach of a statute, or to perpetuate injustice for which the dominant corporation might be liable.[346]

At the same time, the ownership by one corporate entity of all the stock of another does not destroy the separate entity of the subsidiary company, nor give to the dominant corporation the power to act towards the property of its subsidiary as though the latter did not exist.

In his *Principles of Corporation Law,* Mr. France makes a statement of the law which appeals to reason. "According to the weight of authority and reason," he says, "neither the sole owner of the corporation's stock nor a combination of all the owners have any title to the corporate assets which they can convey. Dominant ownership, whether it be fifty-one per cent or ninety-nine per cent of the shares, does not of itself make such owner responsible for the debt of a corporation or prevent him from competing with other creditors in the distribution of assets. It is true that the sole or dominant owner may so conduct himself as to incur personal responsibility, but the doctrine of fraud or estoppel is usually sufficient to meet such cases." "A

[346] Interstate Telegraph Company v. Baltimore and Ohio Telegraph Company of Baltimore County, 51 Fed. 49.

person dealing with a corporation has notice of limited liability."[347]

The well established doctrine is, that the shareholder of a corporation, whether he hold one share or all the shares, has no authority to bind the corporation to any contract which he may make in its behalf merely by reason of his interest in the company.[348]

The Maryland case of Swift v. Smith,[349] as measured by these requirements, cannot be said to lay down a just principle of law, though it may have met the requirements of justice in the particular case. It must be shown that the corporate form has been used as an instrument, tool or agent to commit a fraudulent, illegal, or inequitable act. The mere chance ownership of all the shares by one individual ought never to render the corporation liable for the individual debts or *vice versa*. But it may be said that such a circumstance would warrant the court in scrutinizing the conditions, facts, and surroundings of the dispute and the relation of the parties to the subject-matter in their previous course of dealing.

In the Swift and Smith case a mortgage of corporation chattels, made in his own name by the sole owner of the shares, was upheld against a creditor of the corporation who became such after the shares of stock of the company had been again distributed into the hands of several owners. The mortgage pretended to be a corporate act, and was so understood by the contracting parties. A number of objections were made to its validity as such, because of failure to act in accord with the legal requirements for corporate action. These objections, said the court, "were pressed with much ability and learning, and were fortified with many authorities, which would be conclusive,

[347] France, Principles of Corporation Law, 2nd ed. (1914), par. 17, pp. 22-24, and see Hall Safe Co. v. Herring, etc., Safe Co., 146 Fed. 37, and Warren's Cases on Corporation law, Chap. 3.

[348] 15 Michigan Law Review and fifteen cases there cited.

[349] 65 Md. 428; and see Thompkins v. Sperry, 96 Md. 560; Day v. Postal Co., 66 Md. 369; Morawetz, Corporations, II, sec. 1009.

if the facts and nature of the transaction warranted their application."

"But," said the court, "we think the mortgage to Swift was good, and operative to charge the property conveyed by it, irrespective of the attempted execution by the company." The reason the court gives for this extraordinary statement is that, at the time of its execution, Cruikshank had become the owner of all the stock of the company, and of all its property. "From that moment he might have renounced his rights under the act of incorporation, and might have conducted the business as a private individual without corporate formalities." He had not done so, however; yet the court held that, "being thus absolute proprietor in equity of all that belonged to a purely private enterprise, in which the public had no interest whatever, we know of no principle on the ground of public policy or otherwise, requiring his act in charging the property for the agreed indebtedness of the corporation to Swift for loans to and claims against it, and for his stock in it sold to Cruikshank, to be denied efficacy, because he had not then reorganized the company and brought in other persons to help him to do that in a corporate way which, we think, from the very nature of the business, he had the right to abandon entirely; and even the business if he chose."

Thus the court took the extreme view that "ownership by one person of all the stock of a private corporation aggregate virtually dissolves the corporation," and that "for the time being it certainly does suspend corporate action although, according to the now generally received understanding of the law, such sole owner may dispose of his stock to others and continue the corporate existence by the election of necessary officers."

In thus allowing an individual to share the property of the corporation with his own debts as well as those of the corporate body, by a mortgage that expressly provided for the payment to him individually or his representatives, and not the corporation, of any surplus proceeds after satisfying the mortgage, in

case of sale for default, and then declaring that that mortgage afterward bound a creditor of the corporation who became such after it had been reorganized and some of the stock reissued, the Maryland court has incurred the criticism of the high courts of other states.

In Parker v. Bethel Hotel Company,[350] the Supreme Court of Tennessee refused to consider the decision of the Maryland court as having weight in a similar case, because, it said, "The decision of that learned court is opposed by the current of authorities, and seems to us to overlook and ignore certain principles that are fundamental." It had been argued "that if one person owns all the shares of stock of a corporation which owes no debts, he, in virtue of such ownership, becomes the equitable owner of all of its property, or, at least, may sell and dispose of it by deed, if he chooses to do so." But the court said, and rightly, that, "A corporation and its shareholders are distinct legal entities," and pointed out its previous decision in Keith v. Clark,[351] in which it was held that, "notwithstanding the state owned all the stock in the Bank of Tennessee, the bank and the state are entirely different legal entities."

That the expression of the Tennessee Supreme Court is in accord with the great weight of authority is evidenced by the discussion of the matter of sole ownership of stock of a corporation by a single individual in the Note in L. R. A. under that heading which accompanies Louisville Banking Company v. Eiseman and Company.[352] There attention is called to the fact that "one person cannot conduct his ordinary business in the name of a corporation," nor does the sole owner of the stock of a corporation have such legal ownership of its property that he can maintain replevin therefor in his own name.[353] In the same note it is pointed out that the Supreme Court of Minnesota had held that a deed of corporate property by a sole stock-

[350] 96 Tenn. 255.
[351] 4 Lea (Tenn.), 718; and see Lillard v. Porter, 2 Head, 176.
[352] Ky. (1893), 19 L. R. A. 685.
[353] See Button v. Hoffman, 61 Wis. 20, 50 Am. Rep. 131.

holder in his own name is void on its face and creates no cloud upon the title.[354] Speaking of the decisions in the Maryland case above quoted, the author of the Note says: "The inclination of the Maryland courts seems to be toward a doctrine that is not elsewhere approved."

Important Maryland Cases in which the Corporate Entity Has Been Set Aside. Decisions of a particular state sometimes offer an analytical view of the theories of the nature of the corporation which may profitably be compared with those of the Supreme Court of the United States. Upon a number of points the interpretation of the concepts of the nature of corporate existence set forth in decisions of the Maryland Court of Appeals cannot be said to be in accord with the more advanced reasoning of other courts.

The Maryland cases on the subject of *ultra vires,* and particularly the Western Maryland Railroad Company v. Blue Mountain Hotel Company, have already been refered to. In the case of Swift v. Smith, just discussed, an interpretation by the court of the estoppel doctrine is shown to run counter to the Supreme Court decisions and the decision of Hunter v. Baker Motor Vehicle Company.[355]

The judicial opinion in Pott v. Schmucker[356] has been thought to disregard the corporate entity in the case of a one-man company. It is, however, in no respect necessarily hostile to, or exclusive of, the theory put forward in this study that the doctrines of agency, notice and estoppel are sufficient to meet all possible facts and circumstances without denying distinct reality to the entity. In that case, one member of a partnership formed a corporation of which he was sole owner, and engaged in a separate business of his own. He became in this business a debtor to the firm. In time he became insolvent. It was held

[354] Baldwin v. Canfield, 26 Minn. 43; and see Fitzgerald v. Missouri Pacific Railroad Company, 45 Fed. 812.
[355] 190 Fed. 665, 668 (1911), (C. C. N. D., N. Y.).
[356] 84 Md. 535.

that the firm of which he was a partner was not entitled to share equally with his individual creditors in the distribution of the assets of his separate business. The firm also became insolvent. Although the corporation was the debtor of the firm, it was held that the creditors of the corporation were entitled to priority of payment out of the assets of the corporation as against the trustee in insolvency of the firm.

That case is, however, illustrative of the possible application of the principle according to which a corporation may be charged with the knowledge of a stockholder. Although not adopted by the court's reasoning, this is suggested as a possible ground upon which it might have based its decision to deny the right of a firm to compete with the other creditors of a corporation practically owned by a member of the firm. A member of the firm was also the dominant and, to all intents and purposes, the sole stock owner of the corporation, and had held himself out to the public, while acting in the capacity of director of his corporation, in such a way as to estop him from claiming the right of his firm to participate on an equal footing with the other creditors of his corporation. Both the corporation and the firm would seem, by the decision, estopped to deny their knowledge and sanction of the same individual's acts before the public in the capacity of "sole owner" of the business of the corporation. But the court's statement is unnecessarily broad when it holds that "in a proper case and in furtherance of the ends of justice, (the court) may treat the debtor corporation and the individual owning all its stock and assets as identical." For the court, nevertheless, held that the corporation was a distinct entity, and decided that the trustee of the individuals who owned all of the stock and assets was not entitled to the assets of the corporation.

The case of Bauernschmidt v. Bauernschmidt[357] presents reasoning that is well-nigh inexplicable. The court seems to have made an erroneous application of the general unqualified

[357] 101 Md. 148.

principle that a court, for certain purposes, may disregard the corporate entity. There is in the case no evidence that the corporation is merely an agent used by its incorporators or stockholders to commit fraud or do an illegal act, for the corporation had gone out of existence before the act involved became the subject of dispute; nor was there any ground to assert an estoppel analogous to that in the Schmucker case. The court, almost at random, seems to pick up a catch phrase here and there and apply it. in total disregard of the impossibility of any parallel analogy as to the facts involved which are the determining factors as to whether the general principle of law stated may be correctly applied. Mr. Cook's "Treatise on Corporations" is quoted[358] to the effect that "courts will ignore corporate existence, when necessary in order to circumvent fraud." But the law of the cases upon which Mr. Cook's statement is based, in nearly every instance, is practically all concerned with the deliberate use of the corporate form for the purpose of committing an act which, if done by the individual members of the corporation directly, would be set aside as fraudulent.

It is altogether probable that the court acted upon a broader view of the facts than appears in the reported decisions. The reasoning in respect to the corporation which Mr. Bauernschmidt formed is difficult to comprehend. There are two cases involved in the controversy. In the first one[359] it was not necessary to decide, nor did the court at any time consider the necessity of deciding, to disregard the corporate entity. The only point at issue was whether certain securities still standing in the name of George Bauernschmidt Brewing Company, and found in a safe deposit box to which both Bauernschmidt and his wife had access, were part of Bauernschmidt's estate or belonged to his wife at his death. It was held that they belonged to the estate. As to certain other securities standing also in the name of the George Bauernschmidt Brewing Company, it was

[358] Cook, Corporations, 5th Ed., sec. 317.
[359] *In re* Bauernschmidt, 97 Md. 44.

held that an attempted conveyance of them by the original stockholders of the George Bauernschmidt Brewing Company was no conveyance at all, since the said persons were no longer stockholders of that corporation. They had, during Bauernschmidt's life, transferred all the stock to the Maryland Brewing Company.

In the second case,[360] the question was simply, to whom did certain securities standing in the name of the George Bauernschmidt Brewing Company, but found in the safe deposit box of George Bauernschmidt after his death, belong? The court decided that the original stockholders, since they had transferred all their stock, were in no position to have exercised any control over them, and since the Maryland Brewing Company did not seem to asert any claim on them, the circumstances showed that they belonged to the estate of George Bauernschmidt.

In its two quotations from the first case, the court in the second case made use of statements which had not been used in connection with the question of disregarding the corporate entity, to justify what it thought to be a necessity to so disregard it. It has been pointed out that these statements do not seem to have been well founded. Moreover, the quotation from the case of Seymour v. Spring,[361] brought in to bolster up the second case, does not seem to be in point. In that case there was not a doubt as to the existence of a distinct separate entity, and the New York court held that under the facts asserted it would not be justified in disregarding it.

It must be said, however, that substantial justice was probably done both in the Pott and Schmucker case and in the Bauernschmidt cases.

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[360] 101 Md. 148.
[361] 144 N. Y. 340.

CHAPTER VIII.

CONCLUSION.

It has ever been the aim of American courts to conserve the rights embodied in the Constitution, and the traditions of English common law. If the heritage of ancient doctrine that has enriched American law has at times intensified the conservatism inbred in Bench and Bar, it is with confidence that the people can recognize therein the stability of a legal system that does not change with every passing storm of argument. Practical necessity and public convenience are the guardians of judicial opinion. Particular circumstances focus attention upon special situations, and new sets of facts call forth constant reinterpretation of principles. Into old-established forms of speech new concepts creep. He today who shouts down in ridicule the absurdity of legal fictions may awake tomorrow to find in them the harbingers of progress.

In the administration of justice, the courts must ever seek a compromise. On the one hand, they must meet the requirements of the particular case before them. On the other hand, they must adhere to, and maintain so far as possible, a system of laws based on rational concepts logically related to each other and applicable to the greatest number of similar circumstances in the experience of men. In doing this, they have had to adopt theories of the nature of the corporation and its group life both without and within the law. At times, moreover, changes in economic conditions and in legal concepts have not coincided, and the courts, in the interest of substantial justice, have adopted dogmatic fictions to suit the particular case whose circumstances did not seem to find an adequate remedy in the logical application of old-established theories. These fictions, if they have proved useful, have been retained; and if, perchance, economic

conditions have again changed so that they have become no longer useful, they have gone the way of the concepts which they modified or replaced, and have yielded to statute law or to another fiction more enduring.

Continually in this process the courts have drawn upon the theories of jurisprudence, comparative law, and political philosophy. And just as constantly they have measured these theories by the realities of the objects presented to their scrutiny. The growth in size of corporate undertakings has necessitated this careful process whereby unrealities and fictions which have no beneficial use are compelled to give way to realities. Industry and business demand a more settled condition of the law and a more universal application of doctrines suitable to like circumstances throughout the nation. We have not yet attained this position in all branches of corporation law, but certain aspects of development toward it are discernible.

In Maryland law, the corporation benefits, in some respects, by a more favorable and advanced position taken by the Maryland Court of Appeals, than that found in other jurisdictions. In other respects, however, it still labors under judicial interpretations not in harmony with the more advanced positions taken by courts of other states. Some of these interpretations result from an overconservative hold upon the older theories, while others spring from an unjustifiable disregard of generally accepted doctrines.

In general, it is possible that in the future the public corporation may more and more lose the individuality of group life which characterizes the real corporation, and will become a mere administrative agent of the state. The private corporation will assume increasingly the attributes of autonomy and become emancipated from what must eventually be regarded as an historical fiction—that is, the so-called contractual relation between the corporation and the state. It will take its place as an autonomous unit in the political group in law as it does in fact.

This legal recognition of the yielding of the fiction theory of the nature of the corporation to the realist doctrine is a somewhat radical departure. Only gradually can it be attained. But the day of its coming will mark the achievement of great progress toward the promotion of the administration of that substantial justice which it has ever been the object of Bench and Bar jealously to foster. It will preserve those economic benefits which spring from corporate organization to the individual members of society and to the state itself. Corporate organization is inevitable. Moreover, it is essential to the economic welfare of the nation. Whatever may foster its normal, unfettered growth will benefit both those who engage in business and industry, and the country itself.

Constitutional government aims at certainty in the law. Uniformity is an essential attribute of certainty. To whatever degree these qualities, based upon sound concepts of Jurisprudence and Political Philosophy, may be attained, in like measure will the corporation prosper and the economic and political life of the state expand.

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VITA.

James Treat Carter was born in Platteville, Wisconsin, August 4, 1891, the son of Homer Wright and Jeannie McClelland Carter. In 1892 his family removed to Beloit, Wisconsin. There he received his preparatory education in the public schools and was graduated from Beloit High School in 1909. During the following year he supervised the collections department of the Second National Bank of that city. In 1910 his family removed to Madison, Wisconsin. In the same year he entered Oberlin College, Oberlin, Ohio, from which institution he was graduated with the degree of Bachelor of Arts with Special Honors in Philosophy, in 1914. During the following year he remained in Oberlin as General Secretary of the Oberlin College Young Men's Christian Association, and at the same time pursued post graduate study in English and Political Science. The two years, 1915-1917, he spent in post graduate work in Political Science at The Johns Hopkins University and was twice awarded the University Scholarship. In the summer of 1916 he took post graduate study in Economics, Auditing and Political Science at the University of Wisconsin.

During 1917-1918, while completing his study of Law at the University of Maryland, he acted as secretary to the Chief Judge of the Baltimore Supreme Bench. In August, 1917, he was admitted to the Maryland Bar. On December 26th in that year he was married to Irene Kincaid Morey, daughter of Charles Carroll and Grace Kincaid Morey, of Buffalo, New York. In June, 1918, having completed three years in the study of Law at the University of Maryland, he was graduated with the degree of Bachelor of Laws and awarded the Trial Court and Thesis Prizes. He thereupon undertook the practice of Law in Baltimore, but, on July 2, 1918, entered the service of the United States Army, with the rank of First Lieutenant, in the General Staff, Executive Division, Statistics Branch, and was assigned to duty in the office of the Chief of Staff, Washington, D. C. There he served until March 20, 1919, when he was honorably discharged to resume the practice of Law in Baltimore. In June, 1919, he was awarded the degree of Doctor of Philosophy in Political Science by The Johns Hopkins University.

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This legal recognition of the yielding of the fiction theory of the nature of the corporation to the realist doctrine is a somewhat radical departure. Only gradually can it be attained. But the day of its coming will mark the achievement of great progress toward the promotion of the administration of that substantial justice which it has ever been the object of Bench and Bar jealously to foster. It will preserve those economic benefits which spring from corporate organization to the individual members of society and to the state itself. Corporate organization is inevitable. Moreover, it is essential to the economic welfare of the nation. Whatever may foster its normal, unfettered growth will benefit both those who engage in business and industry, and the country itself.

Constitutional government aims at certainty in the law. Uniformity is an essential attribute of certainty. To whatever degree these qualities, based upon sound concepts of Jurisprudence and Political Philosophy, may be attained, in like measure will the corporation prosper and the economic and political life of the state expand.